REPORT

ON

THE ENFORCEMENT OF JUDGMENT DEBTS AND RELATED MATTERS

ONTARIO LAW REFORM COMMISSION

Ontario

PART IV

Ministry of the
Attorney
General

1983

The Ontario Law Reform Commission was established by section 1 of the *Ontario Law Reform Commission Act*. Section 2(1) of the Act states that it is the function of the Commission to inquire into and consider any matter relating to (a) reform of the law having regard to the statute law, the common law and judicial decisions; (b) the administration of justice; (c) judicial and quasi-judicial procedures under any Act; and (d) any subject referred to it by the Attorney General. The Commissioners are:

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This Report is the fourth in a series of a projected five Part Report. The Honourable J. C. McRuer and the Honourable G. A. Gale were signatories to the first three Parts, but, as will be noted, due to their retirement from the Commission, have not signed this Part. While the Commission benefited greatly from their knowledge and experience, and acknowledges its indebtedness to them, responsibility for the recommendations contained in this Report cannot be attributed to them.

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Ontario
Law Reform
Commission

Ontario

The Honourable R. Roy McMurtry, Q.C.,
Attorney General for Ontario

Dear Mr. Attorney:

We have the honour to submit herewith Part IV of our *Report on the Enforcement of Judgment Debts and Related Matters.*

CHAPTER 1

INTRODUCTION

In 1981, the Commission published the first three Parts of its *Report on the Enforcement of Judgment Debts and Related Matters.* The thrust of our main proposals – the establishment of a new enforcement office with overall responsibility for enforcement matters, and the modernization of the remedies of seizure and sale of a judgment debtor's real and personal property, and of garnishment and receivership – was the need for clarification of, and uniformity in, the law of enforcement. To this end, the Commission made a great many recommendations designed to ensure that, generally speaking, the law of enforcement would be the same with respect to judgments from all court levels, that all of a debtor's property would be available to satisfy a judgment debt, subject to reasonable exemptions, and that the interests of debtors, creditors, and others affected by the enforcement process would be properly balanced. This latter objective is central to the recommendations contained in this Part of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

In Part IV of the Report, we examine two related areas of the law of enforcement: prejudgment remedies and voidable transactions. Both are concerned with the rights of creditors to prevent their debtors from taking steps to frustrate the enforcement of a future or existing judgment debt, as the case may be. For the most part, the relevant legislation has remained unchanged for at least 100 years. In the case of prejudgment remedies, the *Fraudulent Debtors Arrest Act* and, in particular, the *Absconding Debtors Act* do not take full account of legal and technological developments that have occurred since the turn of the century. As a result, the courts in recent years have sought to fill legislative gaps with judicial rules. With respect to Ontario's voidable transactions legislation – the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act* – the courts, in a great number of cases, have superimposed on this legislation so many judicial glosses, many of them conflicting, that no one reading the statutes alone would have a fair or full understanding of the law. As a result, the Commission believes that it is time for a comprehensive and critical review both of the law of prejudgment remedies and of the law of voidable transactions.

CHAPTER 2

PREJUDGMENT REMEDIES

1. INTRODUCTION

To date in its *Report on the Enforcement of Judgment Debts and Related Matters*,[1] the Commission has addressed itself to the reform of postjudgment enforcement remedies, such as the seizure and sale of the judgment debtor's personalty[2] and realty[3] and the garnishment of debts owed to him by a third person.[4] However, in order to create an expeditious, economical and efficacious, yet equitable, enforcement scheme, some prejudgment remedy or remedies also may be required.

Certainly, one of the most frequently voiced criticisms of the present law concerning the enforcement of money judgments is the absence of adequate prejudgment or provisional remedies. If, prior to judgment, the debtor is allowed to denude himself of all his exigible assets with impunity, then the creditor's hard-earned judgment may go for naught. Therefore, it has been suggested, a preoccupation with postjudgment remedies misses the mark: the creditor who has secured a judgment against his debtor may well have won little more than a pyrrhic victory.

Of course, an unsecured creditor may have recourse in appropriate circumstances to a type of "prejudgment relief" under the *Fraudulent Conveyances Act*[5] and the *Assignments and Preferences Act*,[6] a subject that is examined in detail in chapter 3 of this Part of the *Report on the Enforcement of Judgment Debts and Related Matters*. However, reform of the law respecting voidable transactions alone would be inadequate to meet the criticisms respecting the absence in Ontario of effective and comprehensive prejudgment relief legislation. Voidable transactions legislation may assist a creditor to regain property that has been disposed of improperly by his debtor. To some extent, such legislation also may deter debtors from dealing with their property to the detriment of their creditors. Nevertheless, voidable transactions legislation by itself cannot provide a creditor with tangible security for some future judgment; by definition, it is concerned with the rights of a debtor and his creditors after the debtor has put some or all of his property beyond the reach of his creditors. Moreover, it should be pointed out that, even where a creditor is in a position to make use of voidable transactions legislation, the cost of proceeding in this way may be prohibitive in a significant number of cases.

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[1] Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters* (1981) (hereinafter referred to as "Commission Report"), Parts I, II, and III.

[2] Commission Report, *supra*, note 1, Part II, ch. 2.

[3] *Ibid.*, Part III.

[4] *Ibid.*, Part II, ch. 3.

[5] R.S.O. 1980, c. 176.

[6] R.S.O. 1980, c. 33.

Accordingly, in this chapter we focus on the need for, and the appropriate restrictions upon, comprehensive provisional relief legislation in Ontario. We begin with a brief review of certain specialized prejudgment remedies and move on to examine the remedies now generally available to unsecured creditors under Ontario law before judgment. We then consider the approach taken in a number of other jurisdictions to this important area of the law of enforcement. We conclude with a description of some of the reform activity in this area in recent years and with recommendations for reform of the law of provisional relief in Ontario.

2. PREJUDGMENT REMEDIES: THE EXISTING LAW

Our discussion of the existing law is divided into two parts. The first is concerned with a number of specialized prejudgment remedies; the second with the more traditional prejudgment remedies respecting property, such as attachment and garnishment. We should point out that the former are surveyed for comparative purposes only. Consistent with the focus of the *Report on the Enforcement of Judgment Debts and Related Matters* on money judgments, we are concerned in this chapter solely with reform of the more traditional prejudgment remedies available to an unsecured creditor.

(a) SOME SPECIAL PREJUDGMENT REMEDIES

(i) Personal Property Security Act

The *Personal Property Security Act*[7] is concerned, for the most part, with the rights and obligations of persons who are parties to consensual security agreements respecting personal property and fixtures. A brief sketch of remedies under the *Personal Property Security Act* indicates that, at least in this consensual setting, provisional remedies have been sanctioned by the law of Ontario.

Part V of the Act deals with the rights and remedies of, *inter alia*, a secured party upon a default in the performance of the terms and conditions of a security agreement. For example, section 58(*a*) allows a secured party upon default under a security agreement "to take possession of the collateral by any method permitted by law". By virtue of section 59(1), a secured party is empowered to dispose of any collateral upon default. Except where the collateral is perishable or where "the secured party believes on reasonable grounds that the collateral will decline speedily in value", the secured party must give his debtor notice regarding the impending sale of the collateral.[8] The secured party's right to retain or dispose of collateral varies where the "collateral is consumer goods and the debtor has paid at least 60 per cent of the indebtedness secured"[9] thereby.

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[7] R.S.O. 1980, c. 375.

(ii) Replevin

The *Replevin Act*[10] provides that, "[w]here goods, chattels, deeds, bonds, debentures, promissory notes, bills of exchange, books of accounts, papers, writings, valuable securities or other personal property or effects have been wrongfully distrained or have been otherwise wrongfully taken or detained", the owner may maintain an action for replevin for the recovery of the property and for damages.[11] The Act empowers the sheriff in possession of a replevin order to break open a dwelling house[12] or an enclosure[13] to replevy goods, and even to search and examine the person upon whom the property to be replevied is reasonably supposed to be concealed for the purpose of replevying the property in question.[14]

The procedure governing this particular provisional remedy is to be found in the Supreme Court of Ontario Rules of Practice.[15] An order of replevin may be obtained upon a motion or *praecipe*.[16] The latter procedure is available in two situations: (1) where "the property was wrongfully taken out of the possession of the claimant, or fraudulently got out of his possession within two months next before the making of the [supporting] affidavit", *and* "there is good reason to apprehend that, unless the order is issued without waiting for a motion, the delay would materially prejudice the just rights of the claimant with respect to the property";[17] and (2) where the property was distrained for rent or damage feasant and the property was taken under colour of a distress for rent or damage feasant.[18]

Generally speaking, before the sheriff will act on an order of replevin, he will demand from the plaintiff a bond with two sufficient sureties in treble the value of the property as stated in the order.[19] Alternatively, the plaintiff may pay into court twice the value of the goods in dispute.[20] However, the court is given broad powers regarding the making of an order of replevin. For example, a court may require a bond in less or more than treble the value of the property;[21] it may allow the plaintiff, instead of giving a bond, to pay into court "such sum as is proper to stand as security to the defendant";[22] it also may require the sheriff to take and detain the property until further order, rather than at once replevying the property to the plaintiff.[23]

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[8] *Ibid.*, s. 59(5).

[9] *Ibid.*, s. 61.

[10] *Replevin Act*, R.S.O. 1980, c. 449.

[11] *Ibid.*, s. 2.

[12] *Ibid.*, s. 4.

[13] *Ibid.*, s. 5.

[14] *Ibid.*, s. 6.

[15] Supreme Court of Ontario Rules of Practice, R.R.O. 1980, Reg. 540, rr. 359-68 (hereinafter referred to as the "Rules of Practice").

[16] *Ibid.*, r. 359.

[17] *Ibid.*, r. 359(*b*).

[18] *Ibid.*, r. 359(*c*). Damage feasant is defined in *Black's Law Dictionary* (5th ed., 1979), at 351, to mean "[d]oing damage. A term formerly applied to a person's cattle or beasts found upon another's land, doing damage by treading down the grass, grain, etc.".

[19] Rules of Practice, *supra*, note 15, r. 362(1).

[20] *Ibid.*, r. 362(2).

The defendant in a replevin action is given the right to apply to the court to discharge, vary, or modify the order of replevin, to stay the proceedings, or "for any other relief with respect to the return, safety or sale of the property or any part thereof or otherwise".[24] The defendant also will be entitled in certain narrow circumstances to claim damages from the replevying plaintiff.[25]

The *Replevin Act* and the applicable procedural rules are not outlined as a suggested model for prejudgment enforcement remedies. Rather, this provisional remedy is mentioned as one illustration of the law's response to the need for a provisional remedy in a specific context, one that may or may not involve a consensual relationship between plaintiff and defendant.[26]

(iii) Lis Pendens

Although perhaps not always thought of as a prejudgment remedy, a *lis pendens* functions precisely as a provisional remedy. Once registered against the land in dispute,[27] a *lis pendens* serves to put the world on notice of the plaintiff's claim to the land. A *lis pendens* does not prevent the defendant in the action from disposing of the land, although it does make disposition substantially more difficult. Because any purchaser or transferee takes subject to the adjudged rights of the plaintiff, the plaintiff will be in a position to enforce these rights against the purchaser or transferee.

The procedure to be followed in seeking a *lis pendens* is straightforward. Rule 32(2) of the Rules of Practice provides that a plaintiff wishing to obtain a certificate of *lis pendens* must include a claim therefor in the endorsement upon his writ of summons. The claim must include a description of the land sufficient for registration. Application must be made to the court for the issuance of a *lis pendens*, although the Rule permits the application to be made *ex parte*. The certificate of *lis pendens* granted by the court then can be taken and registered against the parcel of land in question.[28]

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[21] *Ibid.*, r. 360.

[22] *Ibid.*

[23] *Ibid.*

[24] *Ibid.*, r. 361.

[25] *Ibid.*, r. 363.

[26] The Civil Procedure Revision Committee, in its review of the Rules of Practice, *supra*, note 15, and *The Judicature Act*, R.S.O. 1970, c. 228, concluded that the matters covered by *The Replevin Act*, R.S.O. 1970, c. 412, were procedural in nature and should be dealt with by *The Judicature Act* rather than by special statute: see Province of Ontario, Ministry of the Attorney General, Civil Procedure Revision Committee, untitled report (June, 1980), at 13; and see s. 51 of Proposed Revision of the Judicature Act (hereinafter referred to as "Williston Committee Revised Judicature Act"), and r. 44 of the Proposed Rules of Civil Procedure (hereinafter referred to as "Williston Committee Rules").

[27] By virtue of section 38 of the *Judicature Act*, R.S.O. 1980, c. 223, a *lis pendens* is available only in actions or proceedings in which "any title to or interest in land is brought in question". The precise meaning of these words has been the subject of substantial litigation. For a compendium of the case law on point, see Hemmerick (ed.), *Holmested and Gale on The Judicature Act of Ontario and Rules of Practice* (Rel. 19, Sept. 1981), para. 4, at 472-73.

The enabling legislation, the *Judicature Act*,[29] also deals with the vacating of a *lis pendens*.[30] Recent amendments to this Act have made "[a]ny person who registers a certificate or caution . . . without a reasonable claim to title or interest in the land . . . liable for any damages sustained by any person as a result of its registration".[31] The issue of liability may be determined upon an application to vacate the *lis pendens*, in the main action in which the question of title to or interest in the land is to be determined, or in a separate action commenced to determine that particular issue.[32]

(iv) Preservation Orders

The Supreme Court of Ontario Rules of Practice contain a number of provisions pursuant to which a claimant can ensure the security of property in dispute pending the final outcome of the litigation.[33] Rule 372, for example, provides in part as follows:

> 372.-(1) The court may, upon the application of any party and upon such terms as seem just, make any order for the detention or preservation of property, being the subject of the action . . . .

A few comments should be made regarding the above Rule. First, it should be noted that the court's power extends to property that is the subject matter of the dispute; therefore, by definition, there must be conflicting claims to the property. Secondly, it is interesting to note that the Rule apparently has generated very little litigation. That this remedy is something akin to a prejudgment remedy is made clear, however, by some of the case law. For example, in one of the leading English decisions concerning preservation orders, *Polini v. Gray*,[34] Jessel M.R. stated the principle underlying the equivalent English Rule to be "that the successful party in the litigation, that is, the ultimately successful party, is to reap the fruits of that litigation, and not obtain merely a barren success".[35]

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[28] See *Judicature Act*, *supra*, note 27, s. 38(1). In the case of land registered under the *Land Titles Act*, R.S.O. 1980, c. 230, a caution would be registered.

[29] *Judicature Act*, *supra*, note 27.

[30] *Ibid.*, s. 39.

[31] *Ibid.*, s. 38(4). This provision was introduced in 1977 (S.O. 1977, c. 51, s. 4(1)) in response to a series of decisions concluding that the filing of a *lis pendens* could not be treated as a slander of title: see, for example, *Greenwood v. Magee* (1977), 15 O.R. (2d) 685, 4 C.P.C. 67 (H.C.J.), and *Aldo v. Dellelce* (1977), 16 O.R. (2d) 490, 2 R.P.R. 41 (H.C.J.).

[32] *Judicature Act*, *supra*, note 27, s. 38(5), also added in 1977 by S.O. 1977, c. 51, s. 4(1). It should be noted that the Civil Procedure Revision Committee has proposed that such a damages claim should be the subject of a counterclaim or a separate action; it should not be a matter determined in the course of a motion to vacate: see Williston Committee Revised Judicature Act, *supra*, note 26, s. 50(5).

[33] *Supra*, note 15, rr. 369-72.

[34] *Polini v. Gray* (1879), 12 Ch. D. 438, 41 L.T. 173 (C.A.) (subsequent reference is to 12 Ch.D.). See, also, *Hofmann v. Hofmann* (1977), 5 B.C.L.R. 204 (S.C.).

Preservation orders would not appear to be granted as a matter of course. Rather, it seems that a plaintiff is required to show at least a *prima facie* right to the property in question.[36] Other factors also may be considered by the court in deciding an application under Rule 372. For example, the likelihood of the property "disappearing" before final adjudication, the possibility of the plaintiff suffering irreparable harm from the loss of the property,[37] and the balance of convenience between opposing parties[38] would appear to be relevant considerations for the court in exercising its discretion under Rule 372.[39]

(v) Statutory and Common Law Liens

While normally not thought of in terms of prejudgment relief, the plethora of liens now extant under Ontario law serves the same function as other prejudgment remedies, that is, to provide a creditor with security for an outstanding debt prior to securing a judgment against the debtor. In the case of some liens, such as mechanics' liens,[40] there may be a substantial connection between the property secured by the lien and the creditor's outstanding claim or debt. In the case of other liens, such as an innkeeper's lien,[41] the relationship between the claim or debt and the secured property may be more tenuous. Common to all such liens is the fact that the legislature or the courts, in a wide variety of circumstances, have seen fit to provide creditors with substantial prejudgment relief.

(vi) Summary

The preceding discussion is not intended to be an exhaustive analysis of the prejudgment remedies considered above. It is meant, however, to show the wide array of prejudgment remedies that now exists in Ontario law outside what are considered to be the traditional enforcement tools — execution, garnishment, and receivership. Granted, these remedies are available in circumstances that may be different from the ordinary action for damages or for the collection of a debt where the parties have not agreed upon any security and where specific property or property interests are not at stake. Nevertheless, there may be a number of reasons, some perhaps even more convincing than those underlying the remedies already considered, for a similar remedy in the case of an ordinary action for damages or for debt. We move now to consider the prejudgment remedies available at the present time to a creditor in an ordinary action.

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[35] *Polini v. Gray*, *supra*, note 34, at 443.

[36] For a recent example of the operation of the merits test, see *Douglas, Rogers Ltd. v. Henderson* (1972), 5 N.S.R. (2d) 396, 28 D.L.R. (3d) 106 (S.C., T.D.), followed in *Carl B. Potter Ltd. v. Anil Canada Ltd.* (1975), 65 D.L.R. (3d) 758 (N.S.S.C., T.D.).

[37] *Douglas, Rogers Ltd. v. Henderson*, *supra*, note 36.

[38] See, for example, *Société pour l'Administration du Droit de Reproduction Mécanique des auteurs, compositeurs et éditeurs (S.D.R.M.) v. Trans World Record Corp.*, [1977] 2 F.C. 602, 17 N.R. 162 (C.A.).

[39] Rule 35.02 of the rules of civil procedure proposed by the Civil Procedure Revision Committee would extend the availability of preservation orders to personal property that is "relevant to any issue in the action": see Williston Committee Rules, *supra*, note 26.

[40] See *Mechanics' Lien Act*, R.S.O. 1980, c. 261. The Act, except for s. 52, is repealed by the *Construction Lien Act, 1983*, Bill 216 (32d Parl. 2d Sess.), which received Third Reading on January 25, 1983, and Royal Assent on January 27, 1983. The new Act is to come into force on April 2, 1983.

[41] See *Innkeepers Act*, R.S.O. 1980, c. 217, ss. 2(1) and 3(1).

(b) THE TRADITIONAL PREJUDGMENT REMEDIES RESPECTING PROPERTY

The more traditional prejudgment remedies are two in number: attachment of the debtor's property, including garnishment of any debts owed to the debtor by a third person, and arrest of the debtor's person. Prejudgment arrest of the debtor — a matter discussed in section 4 of this chapter — is now available only in limited circumstances under the *Fraudulent Debtors Arrest Act*[42] and section 24 of the *Family Law Reform Act*.[43] Attachment, or seizure of the debtor's property, before judgment is authorized by the *Absconding Debtors Act*[44] and by the absconding debtors provisions of the *Small Claims Courts Act*.[45] Under the former, a creditor may reach all his debtor's assets, including debts owed to the debtor by a third person. Until the amendment of *The Small Claims Courts Act*[46] in 1977, separate remedies were used to reach property and debts under that Act. Exigible property could be attached; debts had to be garnished. Although the prejudgment garnishment provisions of *The Small Claims Courts Act* were repealed in 1977,[47] in order to be comprehensive, we shall include a discussion of this remedy in our review of the traditional prejudgment remedies.

(i) Attachment

a. A Brief History

It is generally agreed that the progenitor of the attachment process was the ancient custom of foreign attachment.[48] To overcome the problems of asserting jurisdiction over a foreign debtor, certain municipal courts, such as the Mayor's Court of London, allowed a creditor of a foreign debtor to attach debts owing to the debtor by persons within the jurisdiction of the court. In this way, a creditor could compel his debtor to return to the jurisdiction and make himself subject to mesne process[49] or risk losing the money attached. Drake, in his treatise on attachment, makes the following comparison between the procedure for foreign attachment and that followed in an ordinary action for the recovery of a debt:[50]

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[42] *Fraudulent Debtors Arrest Act*, R.S.O. 1980, c. 177.

[43] *Family Law Reform Act*, R.S.O. 1980, c. 152.

[44] *Absconding Debtors Act*, R.S.O. 1980, c. 2.

[45] *Small Claims Courts Act*, R.S.O. 1980, c. 476, ss. 159 *et seq.*

[46] R.S.O. 1970, c. 439.

[47] *The Small Claims Courts Amendment Act, 1977*, S.O. 1977, c. 52, s. 16.

[48] For a general discussion of foreign attachment, see Drake, *A Treatise on the Law of Suits by Attachment in the United States* (7th ed., 1891), ch. 1; Millar, *Civil Procedure of the Trial Court in Historical Perspective* (1952), ch. XXVI; and Dunlop, *Creditor-Debtor Law in Canada* (1981), at 196-97. See, also, *The Mayor and Aldermen of the City of London v. Cox* (1867), L.R. 2 H.L. 239, 16 W.R. 44.

[49] Such as prejudgment arrest pursuant to the writ of *capias ad respondendum*.

> At common law the first step in an action, without which no other can be taken, is to obtain service of process on the defendant; under the custom, this is not only not done, but it was declared by Lord Mansfield, that the very essence of the custom is that the defendant shall not have notice. At common law a debtor's property can be reached for the payment of his debt, only under a *fieri facias*; under the custom, it is subjected to a preliminary attachment, under which it is so held as to deprive the owner of control over it, until the plaintiff's claim be secured or satisfied. At common law only tangible property can be subjected to execution; under the custom, a debt due to the defendant is attached, and appropriated to the payment of his debt. At common law, after obtaining judgment, the plaintiff is entitled to execution without any further act on his part; under the custom, he cannot have execution of the garnishee's debt, without giving pledges to refund to the defendant the amount paid by the garnishee, if the defendant, within a year and a day, appear and disprove the debt for which the attachment is obtained.

Although employed well into the latter half of the nineteenth century, for a variety of reasons foreign attachment since has become redundant and unimportant in England.[51]

There does not appear to be any evidence that the doctrine of foreign attachment ever took root in Ontario. Indeed, in 1832, special legislation was introduced in Upper Canada in order to provide relief to a creditor whose debtor had left the jurisdiction, leaving behind property and debts owed to him by third persons in the jurisdiction.[52]

When enacted, the legislation served two purposes. It afforded "the means of attaching the Property of Absconding Debtors, that the same may be taken in Execution and sold for the benefit of their Creditors". In other words, the legislation served a security function, enabling a creditor in certain circumstances to gain security for his future judgment against the debtor, by allowing him to gain control of his debtor's property or part of his property.

However, the 1832 Act also served another important function, that is to say, a jurisdictional function. It should be noted that, until 1856,[53] there was no means by which a court in Upper Canada could assert jurisdiction over any person who could not be served in the jurisdiction with originating process and who did not submit to the jurisdiction of the court.[54] Where the debtor was outside the territorial jurisdiction of the court, arrest on mesne process was not possible. As a result, the attachment of an absconding debtor's property could be used to encourage the debtor to return to the jurisdiction and to subject himself to local process.

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[50] Drake, *supra*, note 48, at 3.

[51] For a good discussion of the demise of foreign attachment in England, see Levy, "Attachment, Garnishment and Garnishment Execution: Some American Problems Considered in the Light of the English Experience" (1972-73), 5 Conn. L. Rev. 399.

[52] *An Act to afford means for attaching the Property of Absconding Debtors*, 2 Wm. 4, c. 5 (U.C.). The Act's preamble reads as follows:

> Whereas it is necessary, for the protection of persons engaged in trade, to afford the means of attaching the Property of Absconding Debtors, that the same may be taken in Execution and sold for the benefit of their Creditors. . . .

[53] See the *Common Law Procedure Act, 1856*, 19 Vict., c. 43 (U.C.), ss. 43-47. Service *ex juris* now is governed by rr. 25-31 of the Rules of Practice, *supra*, note 15.

Before appearing in the Consolidated Statutes of Upper Canada in 1859,[55] the 1832 legislation was amended a number of times. The last major revision of what now is known as the *Absconding Debtors Act* occurred in 1909,[56] and since that time the Act has remained essentially unchanged.

Attachment proceedings against an absconding debtor also may be brought pursuant to the *Small Claims Courts Act*,[57] a jurisdiction that these courts and their predecessors have enjoyed since 1849.[58] Although the absconding debtors provisions of the *Small Claims Courts Act* are quite similar to those found in the *Absconding Debtors Act*, there are some important jurisdictional and procedural differences. Accordingly, we now turn to consider the statutory scheme of Ontario's present absconding debtors legislation.

b. The Statutory Scheme

To determine the ambit of the *Absconding Debtors Act*, sections 2(1) and 3(1) of the Act must be read together. Section 2(1) provides as follows:

> 2.-(1) Where a person resident in Ontario departs therefrom with intent to defraud his creditors or any of them, or to avoid being arrested or served with process, being then possessed of any real or personal property therein not exempt by law from seizure under execution, he shall be deemed an absconding debtor, and such property may be seized and taken by an order of attachment for the satisfying of his debts.

While section 2(1) refers to a person who "departs" from Ontario, section 3(1) states that an applicant must swear that he "has good reason to believe and does believe that [his debtor] *has departed* from Ontario".[59] Notwithstanding the wording of section 2(1), it would appear that a creditor cannot seek prejudgment relief under the Act if his debtor is preparing to leave, but has not yet left, the jurisdiction.[60] Moreover, only a person who has departed from the Province with the requisite intent may have his property "seized and taken by an order of attachment for the satisfying of his debts". In other words, unless a person has departed either "with the intent to defraud his creditors or any of them" or in order "to avoid being arrested or served with process", he is not subject to the rigours of the Act.

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[54] See Castel, *Canadian Conflict of Laws* (1975), Vol. I, ch. 9, and Morris (ed.), *Dicey and Morris on The Conflict of Laws* (9th ed., 1973), at 158 *et seq.*

[55] C.S.U.C. 1859, c. 25.

[56] *The Absconding Debtors Act*, 9 Edw. 7, c. 49. The Act appeared in the 1877, 1887, and 1897 revisions as chapter 68, 66, and 79, respectively.

[57] *Supra*, note 45.

[58] *An Act to authorize Attachments against Personal Property, for sums of ten pounds and under in certain cases in Upper Canada*, 12 Vict., c. 69 (S.P.C.) was passed "to provide further protection to Creditors, and to afford the means of attaching the personal property of absconding, removing or concealed Debtors in Upper Canada, for any sum to the amount of ten pounds, and not less than twenty shillings, for any debt or damage arising upon any contract express or implied, or upon any judgment".

[59] Emphasis added.

Sections 2(1) and 3(1) of the *Absconding Debtors Act* should be contrasted with section 159 of the *Small Claims Courts Act*. Section 159 reads as follows:

> 159. Where a person indebted in a sum not less than $4, either for debt or damages arising upon a contract, and recoverable in or upon a judgment of a small claims court,
>
> (*a*) absconds from Ontario, leaving personal property liable to seizure under execution for debt in any county; or
>
> (*b*) attempts to remove such personal property out of Ontario or from one county to another therein with intent to defraud; or
>
> (*c*) keeps himself concealed to avoid service of process,
>
> the clerk of any small claims court, upon the application of the creditor and upon his filing an affidavit in the prescribed form made by him, his agent or servant, shall issue a warrant in the prescribed form, directed to the bailiff of the court from which it issued, or to a constable of the county, commanding him to attach, seize, take and safely keep all the personal estate and effects of such person in the county, liable to seizure under execution for debt, or a sufficient part thereof to secure the sum mentioned in the warrant with costs, and to return the warrant forthwith to the court.

A number of comments should be made regarding the grounds for attachment set out in section 159. First, a literal reading of the section would suggest that a warrant of attachment may be secured even where the debtor is in the process of departing from Ontario. Secondly, it would seem that a creditor relying on this ground for attachment would not have to establish an intent to defraud. Yet, the affidavit that is required to be filed in support of an application for a warrant of attachment includes the following statement:[61]

> That I have good reason to believe and do verily believe that the said . . ., *with intent and design to defraud* me (*or* the said . . .) of my (*or* his) said debt, *has absconded* from this province . . . .

Thirdly, it may be argued that, although attempts to remove his personal property from Ontario will be sufficient to subject a debtor to the attachment remedy, a debtor who has actually removed his personal property from the Province would remain immune. Finally, while the wording of section 159(*c*) suggests that a creditor who relies on the fact that his debtor has concealed himself to avoid process does not have to show an intent to defraud on the part of his debtor, the supporting affidavit prescribed by regulation does make reference to the debtor's "intent and design to defraud".[62]

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[60] See Dunlop, *supra*, note 48, at 206.

[61] Rules of Procedure, R.R.O. 1980, Reg. 917, r. 69, Form 57 (emphasis added).

Having set out the grounds for attachment under the *Absconding Debtors Act* and the *Small Claims Courts Act*, we shall now sketch the other substantive statutory requirements that must be satisfied before an order or warrant of attachment may issue under these Acts. Under the former, for example, the prejudgment remedy of attachment is available only against persons resident in Ontario at the time of their departure.[63] No similar limitation can be found in the absconding debtors provisions of the *Small Claims Courts Act*. Similarly, while an order of attachment pursuant to the *Absconding Debtors Act* may be made "only in a pending action",[64] a creditor seeking a warrant of attachment under the *Small Claims Courts Act* need not have instituted separate legal proceedings before a warrant will issue: the action may be commenced by the attachment proceedings themselves.[65]

It is not every creditor that can take advantage of the prejudgment remedy of attachment. In the case of attachment under the *Absconding Debtors Act*, the debtor must be indebted to the applicant in a sum in excess of $100.[66] Only a creditor claiming that his debtor is "justly and truly indebted"[67] to him may be granted a warrant of attachment under the *Small Claims Courts Act*. The Act also provides that the indebtedness must be a sum "not less than $4, either for debt or damages arising upon a contract, and recoverable in or upon a judgment of a small claims court".[68] Consequently, a damages claim sounding in tort clearly would not support an application for either an order or a warrant of attachment.

The procedures for securing an order and warrant of attachment are quite similar. In each case, the applicant must file an affidavit sworn either by himself or by his agent.[69] With respect to proceedings instituted pursuant to the *Absconding Debtors Act*, the affidavit must state the following: (1) that the debtor is indebted to the creditor in a sum exceeding $100; (2) the cause of action; (3) that the deponent has good reason to believe and does believe that the debtor has departed from Ontario with the requisite intent; and (4) that at the time that he departed the debtor was possessed to his own benefit of real or personal property in Ontario not exempt by law from seizure under execution.

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[62] *Ibid.*

[63] See s. 2(1) of the *Absconding Debtors Act*, *supra*, note 44, set out *supra*, at 11.

[64] See s. 2(2) of the Act.

[65] See s. 162 of the *Small Claims Courts Act*, *supra*, note 45, and Rules of Procedure, *supra*, note 61, r. 41.

[66] *Supra*, note 44, s. 3(1).

[67] Rules of Procedure, *supra*, note 61, r. 69, Form 57.

[68] *Supra*, note 45, s. 159.

[69] See *Absconding Debtors Act*, *supra*, note 44, s. 3(1), and *Small Claims Courts Act*, *supra*, note 45, s. 159. Under the latter, a servant of the applicant also may swear the necessary affidavit.

In addition to his own affidavit (or an affidavit sworn by his agent), an applicant for an order of attachment must file the affidavits of two persons able to swear that they are well acquainted with the debtor and that they have good reason to believe and do believe that he has departed with the requisite intent.[70] The affidavit prescribed by regulation for use in respect of attachment proceedings in the small claims courts touches upon the same matters referred to in items (1) to (4), above.[71]

Both statutes permit an application for prejudgment relief in the form of attachment to be made *ex parte*. Under the terms of the *Small Claims Courts Act*, the application may be made to the clerk of a small claims court. If the clerk receives an application with an affidavit in the prescribed form, it would appear that he must issue a warrant of attachment.[72] In the alternative, a creditor may take his application before a judge or justice of the peace, who, in his discretion, may issue a warrant of attachment.[73] In the case of attachment under the *Absconding Debtors Act*, the application must be made to a judge of the Supreme Court or of a county or district court, depending on the amount claimed by the creditor.[74]

Once an order or warrant of attachment has issued, the creditor must deliver it to the sheriff, bailiff, or constable, as the case may be, for execution. Under the *Absconding Debtors Act*, a copy of the order of attachment must be served upon the debtor.[75] No such duty is imposed by the *Small Claims Courts Act*. The duties of a sheriff, bailiff, or constable in receipt of an order or warrant of attachment are similar: he must execute the order or warrant immediately and then prepare an inventory of all the attached property.[76]

What property is liable to be seized under an order or warrant of attachment? In this respect, the two statutes under consideration do differ substantially. Under the *Small Claims Courts Act*, only the personal estate and effects of the debtor are subject to attachment.[77] Section 7 of the *Absconding Debtors Act*, on the other hand, speaks in terms of "[a]ll the property of an absconding debtor", both real and personal, including debts owed to the debtor by third persons.[78] Only property that is liable to seizure under execution may be attached; property that is exempt by law from seizure under execution is also exempt from seizure under attachment.[79] It should be noted that, under the *Absconding Debtors Act*, a sheriff may demand, and is entitled to receive, any property belonging to the debtor, or the proceeds thereof, in the custody of a constable or bailiff or clerk of a small claims court under a warrant of attachment, or money paid into court under a garnishment summons under the *Small Claims Courts Act*,[80] to be distributed in due course pursuant to the *Creditors' Relief Act*.[81]

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[70] *Absconding Debtors Act*, *supra*, note 44, s. 3(1).

[71] See Rules of Procedure, *supra*, note 61.

[72] *Supra*, note 45, s. 159.

[73] *Ibid.*, s. 160. "Judge" is defined in the Act to mean "a small claims court judge appointed under this Act" or "a judge of a county court": see s. 1(*h*).

[74] *Absconding Debtors Act*, *supra*, note 44, s. 3(1) and (2).

[75] *Ibid.*, s. 4.

[76] See *Absconding Debtors Act*, *supra*, note 44, s. 7, and *Small Claims Courts Act*, *supra*, note 45, s. 161. It should be noted that a constable executing a warrant of attachment is required to deliver any property that he has seized "to the bailiff of the court out of which the warrant of attachment issued or into which it was made returnable": see s. 168(1) of the *Small Claims Courts Act*.

[77] *Supra*, note 45, ss. 159 and 161.

Although property taken pursuant to an order or warrant of attachment may be sold prior to judgment, the primary obligation of the attaching officer is to hold on to the property. It would appear that a bailiff may retain property taken under a warrant of attachment until judgment in the main action has been rendered. On the other hand, under section 18 of the *Absconding Debtors Act*, unless a writ of execution is placed in the sheriff's hands for execution within three months of the making of the order of attachment, the sheriff must return all the attached property and any proceeds realized from the sale of such property.[82]

Insofar as the sale of property seized under an order or warrant of attachment is concerned, there are two situations in which sale before judgment is possible. First, certain types of property may be sold without court approval. Section 8 of the *Absconding Debtors Act* provides as follows:

> 8.-(1) Where horses, cattle, sheep or pigs, or perishable property, or such as from its nature cannot be safely kept or conveniently taken care of, are taken under an order of attachment, the sheriff who attaches them shall have them appraised, on oath, by two competent persons, and, if the plaintiff desires it and deposits with the sheriff a bond to the defendant executed by two freeholders, approved as sufficient by the sheriff, in double the appraised value of the property, conditioned for the payment of the appraised value to the defendant, his executors or administrators, together with all costs and damages incurred by the seizure and sale thereof, in case judgment is not obtained by the plaintiff against the defendant, then the sheriff shall proceed to sell all or any of such property at public auction to the highest bidder, giving not less than six days notice of the sale, unless any of the property is of such a nature as not to allow of that delay, in which case the sheriff may sell it forthwith, and the sheriff shall hold the proceeds for the same purposes as he would hold property seized under the order of attachment.
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> (2) If the plaintiff, after notice to him or to his solicitor of the seizure of any

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[78] *Supra*, note 44, s. 14.

[79] See *Absconding Debtors Act*, *supra*, note 44, s. 7, and *Small Claims Courts Act*, *supra*, note 45, s. 159. See Dunlop, *supra*, note 48, at 208-10, where this matter is discussed.

[80] *Supra*, note 44, s. 9. The term garnishment summons is a reference to the prejudgment garnishment procedure formerly available under the *Small Claims Courts Act*. We examine prejudgment garnishment *infra*, sec. 2(b)(ii).

[81] *Creditors' Relief Act*, R.S.O. 1980, c. 103. See *infra*, this sec.

[82] This three month period may be extended by an order of the court under section 18.

> property mentioned in subsection (1), does not deposit such bond, then, after four days next after the notice, the sheriff is relieved from all liability to the plaintiff in respect of the property so seized, and the sheriff shall forthwith restore it to the person from whose possession it was taken.

Sections 171 and 172(1) of the *Small Claims Courts Act* read as follows:

> 171. Subject to the *Absconding Debtors Act*, where perishable property has been attached, the bailiff who has the custody thereof, it having been first appraised, may, at the request of the attaching creditor, expose and sell it at public auction to the highest bidder, giving at least eight days notice, at the office of the clerk and at two other public places in his division, of the time and place of sale, if the property attached will admit of being so long kept, otherwise he may sell it at his discretion.
>
> 172.-(1) It is not compulsory upon the bailiff or constable to attach, or upon the bailiff to sell, perishable property until the attaching creditor has given a bond to the defendant, with good and sufficient sureties to the satisfaction of the bailiff, in double the amount of the appraised value of the property, conditioned that the attaching creditor will repay the value thereof, together with all costs and damages incurred in consequence of the attachment and sale, in case judgment is not obtained by him, and the bond shall be filed with the clerk.

The first point that should be made about these sale provisions concerns their ambit. Only "perishable property" may be sold prior to judgment under section 171. Section 8(1) of the *Absconding Debtors Act*, in contrast, speaks of "horses, cattle, sheep or pigs, or perishable property, or such as from its nature cannot be safely kept or conveniently taken care of". Secondly, it should be pointed out that, while a bond from the attaching creditor in favour of the debtor is discretionary under the *Small Claims Courts Act*, it would seem to be mandatory under section 8 of the *Absconding Debtors Act*. Thirdly, in each case, notice of the sale must be given and the sale must be by way of a public auction, unless the nature of the property requires immediate sale. Fourthly, under both statutes, before sale, the sheriff or bailiff, as the case may be, must have the property appraised. And finally, the creditor's bond must be in double the appraised value of the property.

The second situation in which attached property may be sold prior to judgment is dealt with in section 12(2) of the *Absconding Debtors Act*.[83] Section 12(1) of that Act, like the *Small Claims Courts Act*,[84] allows a debtor to regain possession of any of his property upon certain terms, including the filing of a bond in double the appraised value of the property. Section 12(2) of the *Absconding Debtors Act* provides that, "[i]f within one month after the property has been attached such bond is not executed and filed," sale of "any of the goods and chattels that have been attached, except chattels real" may be ordered by the court.

Distribution to the attaching creditor of the proceeds realized from the sale of any attached property must await final judgment against the debtor. An order of attachment or a warrant of attachment is used simply to secure sufficient of the debtor's assets to satisfy a future judgment; it is the judgment and initiation of enforcement proceedings that entitle the creditor to apply the attached property or the proceeds thereof in satisfaction of the outstanding judgment debt.

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[83] *Supra*, note 44.

[84] *Supra*, note 45, s. 169(1).

Under the *Small Claims Courts Act*, where there is only one attachment against a debtor, "[t]he property attached . . . is liable to seizure and sale under the execution to be issued upon the judgment, and . . . the proceeds thereof shall be applied in satisfaction of the judgment".[85] Where there are a number of attachments against a single debtor, section 166 of the Act provides that "the proceeds of the property attached shall not be paid over to the attaching creditors according to priority, but shall be rateably distributed among such of them as obtain judgment against the debtor". The section goes on to state that "no distribution shall take place until, in the opinion of the judge, reasonable time has been allowed to the creditors to proceed to judgment". This scheme of rateable distribution is an exception to the priority regime that normally prevails in the small claims courts.[86]

The proceeds from the property of a debtor against whom an order of attachment has been issued under the *Absconding Debtors Act* are subject to the scheme of rateable distribution outlined in the *Creditors' Relief Act*.[87] Unless the attaching creditor delivers to the sheriff a writ of execution or certificate of proof of claim within two months from the time the sheriff first received such proceeds, the creditor will not be entitled to share in their distribution under the *Creditors' Relief Act*.[88] It should be noted that, under section 21(1) of the *Creditors' Relief Act*, an attaching creditor is entitled to a priority in respect of the costs of the order of attachment and "the proceedings thereon".

c. *The Jurisprudence*

Although prejudgment attachment of the property of an absconding debtor has been available in this jurisdiction for 150 years, reported cases have been few and far between. At first glance, the dearth of legal authority may be somewhat surprising. However, given the narrow scope of the remedy and the chilling judicial reception that the *Absconding Debtors Act* and similar statutes in other Canadian jurisdictions[89] have received, the paucity of authorities is quite understandable. In this section, we turn our attention to an analysis of the judicial interpretation and the practical operation of Ontario's absconding debtors legislation, with frequent reference to the decisions respecting similar legislation in other provinces.

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[85] *Ibid.*, s. 164.

[86] See the discussion of the scheme of distribution applicable to the proceeds of enforcement from the small claims courts in Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

[87] *Supra*, note 81, s. 5(1), which reads as follows:

> 5.-(1) Where a sheriff levies money under an execution against the property of a debtor or receives money in respect of a debt that has been attached or sold under section 15 of the *Absconding Debtors Act*, he shall forthwith make an entry in Form 1 in a book to be kept in his office, and such book shall be open to the public for inspection without charge.

The wording of this section is far from satisfactory, since it may be interpreted to mean that the sheriff need make an entry only for money received in respect of a debt sold under section 15 of the *Absconding Debtors Act*, but not for the proceeds realized on the sale of attached property. See, also, s. 21(1) of the the *Creditors' Relief Act*. The *Creditors' Relief Act* will be examined in detail in Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

[88] See subsections (2) and (12) of section 5 of the *Creditors' Relief Act*, *supra*, note 81.

(1) *General Considerations*

While recognizing both the security function and the jurisdictional function[90] of absconding debtors legislation, courts in this country have been reluctant to give the legislation a "fair, large and liberal construction and interpretation".[91] The legislation, generally speaking, has been perceived by the courts as being unusual, and as providing creditors with a remedy that was not available at common law and that could have serious consequences for debtors. The view of Richards J.A., in *McIntyre v. Gibson*,[92] seems to be typical of the judicial perception of prejudgment attachment under absconding debtors legislation:[93]

> The remedy is a harsh one from the defendant's point of view. It ties up what may chance to be all of his means, and may work a great hardship to him.

Given this sort of assessment of the legislation, it is not surprising that the courts consistently have adopted a strict constructionist approach to this "extraordinary remedy",[94] demanding "strict compliance with all the statutory requirements".[95]

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[89] Alta: Alberta Rules of Court, Alta. Reg. 390/68, as am., rr.485-93; B.C.: *Absconding Debtors Act*, R.S.B.C. 1960, c. 1, repealed by S.B.C. 1978, c. 11, s. 1; Man.: Manitoba Queen's Bench Rules, Man. Reg. 26/45, as am., rr. 582-619; N.B.: *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2; Nfld.: *The Judicature Act*, R.S.N. 1970, c. 187, ss. 82-99; N.S.: Nova Scotia Civil Procedure Rules and Related Rules, r. 49 (hereinafter referred to as "Nova Scotia Rules"); P.E.I.: Prince Edward Island Rules of Court, r. 49 (hereinafter referred to as "Prince Edward Island Rules"); Que.: *Code of Civil Procedure*, R.S.Q. 1977, c. C-25, arts. 733-41; and Sask.: *The Absconding Debtors Act*, R.S.S. 1978, c. A-2.

[90] See, for example, *Kingsmill v. Warrener* (1852), 13 U.C.Q.B. 18 (C.A.), *per* Burns J., aff'g (1852), 8 U.C.Q.B. 407.

[91] See s. 10 of the *Interpretation Act*, R.S.O. 1980, c. 219.

[92] (1908), 8 W.L.R. 202, 17 Man. R. 423 (C.A.) (subsequent references are to 8 W.L.R.).

[93] *Ibid.*, at 204. See, also, *Dow v. Dayment*, [1923] 1 D.L.R. 772, [1922] 3 W.W.R. 1119 (Man. C.A.), at 1125, *per* Dennistoun J.A.

[94] *Safety Freight Ltd. v. Orr*, [1955] 1 D.L.R. 714, (1954), 14 W.W.R. 24 (Man. C.A.).

[95] *Lukian v. Shankoff*, [1945] 1 W.W.R. 345 (Sask. Q.B.); *Safety Freight Ltd. v. Orr*, *supra*, note 94; and *Hart v. Cunningham* (1898), 40 N.S.R. 229 (S.C.). Compare *Re Atlantic Pet Food Supply Inc.* (1977), 19 N.B.R. (2d) 602, at 609, 30 A.P.R. 602 (S.C., Q.B.), at 609, *per* Richard J., rev'd on other grounds (1978), 22 N.B.R. (2d) 81, 39 A.P.R. 81 (S.C., App. Div.):

> Looking into the general purpose of the Act [*Absconding Debtors Act*, R.S.N.B. 1973, c. A-2], I would have to conclude that it is remedial and enlarging in nature. Unlike the *Arrest and Examinations Act* which provides for the issue of a capias and accordingly the deprivation of liberty of a subject, and therefore re-

A few comments should be made at this point regarding the effect of an order or warrant of attachment. The courts have emphasized the security implications of such an order or warrant, holding that an attaching creditor merely acquires a security or "lien" for his claim.[96] Therefore, unless the plaintiff in his action against the absconding debtor proves his claim, and obtains judgment and a writ of execution, "his attachment avails nothing".[97]

When does the "lien" created by attachment take effect? It would seem that the attachment order is only effective once the sheriff or bailiff seizes the property in question. Mere issuance of the order or warrant has been held not to be sufficient.[98] Nor has delivery of an order or warrant of attachment to the sheriff been considered to put the property beyond the power of the debtor.[99] Only physical seizure[100] or its equivalent[101] would seem to put the attached property beyond the debtor's control.

Insofar as the property that may be affected by attachment is concerned, we already have made reference to the fact that, under the *Absconding Debtors Act*, all the debtor's property, both real and personal, may be seized under an order of attachment, but only the debtor's personal estate and effects may be taken under a warrant of attachment issued pursuant to the *Small Claims Courts Act*.[102] The debtor's property may be seized whether in the custody or possession of the debtor himself or a third person.[103]

However, as a result of two early New Brunswick cases,[104] there may be some doubt whether property acquired after the issuance of an attachment order may be seized under the order. This issue does not seem to have arisen in any other jurisdiction, and it may well be that these authorities are outdated and anomalous.

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quires very strict compliance and interpretation, this Act on the contrary ought to be, whenever it is reasonable to do so, given an interpretation commensurate to its general purpose of extending the common law protection already given to genuine creditors of our province.

[96] *Stairs, Son & Morrow v. Neilson* (1920), 56 D.L.R. 674, at 675, 54 N.S.R. 114 (S.C.), *per* Harris C.J. The creditor is not a lienholder, in the sense that he is entitled to an interest in the property: see Dunlop, *supra*, note 48, at 199 *et seq.*

[97] *Rumsey v. Hare* (1877), 12 N.S.R. 4 (S.C.), at 8. See, also, *Stairs, Son & Morrow v. Neilson*, *supra*, note 96.

[98] *Kingsmill v. Warrener*, *supra*, note 90.

[99] *Kingsmill v. Warrener*, *ibid.*, *per* Burns J. and Spragge V.C.; *Taylor (Sheriff) v. Brown* (1867), 17 U.C.C.P. 387; and *Robinson v. Bergin* (1883), 10 P.R. 127 (S.C.O. Master).

[100] *Kingsmill v. Warrener*, *supra*, note 90. See, also, *Mahon v. Crowe* (1896), 28 N.S.R. 250 (S.C.), and *Potter v. Carroll* (1860), 9 U.C.C.P. 442, aff'd 1 E. & A. 341.

[101] See, for example, *Bank of Montreal v. Wallace* (1906), 1 E.L.R. 228 (N.S.) (levy effected against real property by registration).

[102] See discussion *supra*, sec. 2(b)(i)b.

[103] See, for example, *Buntin v. Williams* (1894), 16 P.R. 43 (Ch.D.) (property in the hands of the debtor's solicitor).

[104] *Hanington v. Harshman* (1873), 14 N.B.R. 217 (S.C.), and *Cullen v. Voss* (1875), 15 N.B.R. 464 (S.C.).

(2) *Conditions for Attachment: Nature of the Plaintiff's Claim*

We have mentioned the fact that one of the conditions for resort to Ontario's absconding debtors legislation is a claim that the debtor is "indebted" to the applicant.[105] What kinds of legal obligation does the word "indebted" cover?

In the early case of *Clark v. Ashfield*,[106] the Court took a narrow view of the ambit of the 1832 Act. It was held in that case that a claim for unliquidated damages could not support an order of attachment. Another example of the strict constructionist attitude can be seen in the decision of *Taylor v. Nicholl*.[107] There the defendant gave the plaintiff a note payable at a future time, and shortly thereafter left Ontario and returned to Scotland where he resided. The Court stated that, at the time he left the jurisdiction, the defendant was not a debtor for the purpose of the Ontario absconding debtors statute. Presumably, this conclusion was based on the fact that there was no debt due and owing at the time the defendant departed. If the Ontario courts were to follow this case today, there would be an obvious gap in the prejudgment remedy of attachment. In *Kyle v. Barnes*,[108] the Court went one step further, stating that the statute "does not warrant the issue of an attachment where the debt or indebtedness is not presently payable, though there may be a present indebtedness without any right in the creditor to present payment".[109]

In some jurisdictions, the absconding debtors legislation would seem to be somewhat broader. For instance, the attachment provisions of the Manitoba Queen's Bench Rules apply where a person is "indebted or *legally liable* to a creditor either in respect of a contract, express or implied, made in Manitoba, or in respect of any cause of action arising therein, or in case of a contract or other obligation, if made elsewhere, to be performed or partly performed in Manitoba, or *liable to be compensated for in damages*, or in respect of a cause of action which arose or partly arose and for which he is liable to satisfy another person in Manitoba".[110] However, the courts have construed this key provision narrowly. In *Hime v. Coulthard*,[111] for example, the Court concluded that the attachment procedure prescribed by the rules of practice was available only in respect of contractual, as opposed to tortious, claims. The basis for this finding was the view of the Court that a tort claimant could not provide an affidavit stating "that the debtor is justly and truly indebted to the creditor, or is legally liable to him in damages, in [the sum claimed], after making all proper and just set-offs, allowances, and discounts",[112] as required by the rules of practice. It is hard to see how a person seeking damages for breach of contract would be in any better position than a tort claimant in providing the requisite affidavit. What this case and the Ontario decisions would seem to indicate is, as suggested earlier, a judicial reluctance to give attachment legislation a broad and liberal interpretation.

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[105] See s. 3(1) of the *Absconding Debtors Act*, *supra*, note 44, and s. 159 of the *Small Claims Courts Act*, *supra*, note 45.

[106] (1837), 1 Ont. Case Law Digest 192.

[107] (1844), 1 U.C.Q.B. 416.

[108] (1883), 10 P.R. 20 (H.C.J.).

[109] *Ibid.*, at 24. The problem of debts due but not payable has been addressed in two Canadian jurisdictions by an express provision overruling *Kyle v. Barnes*: see Nova Scotia Rules, r. 49.01(3), and Prince Edward Island Rules, r. 49.01(3).

[110] Manitoba Queen's Bench Rules, *supra*, note 89, r. 582(b) (emphasis added).

[111] (1910), 15 W.L.R. 288, 20 Man. R. 164 (K.B.).

(3) *Conditions for Attachment: Jurisdiction*

An issue related to the nature of the plaintiff's claim is the requirement that the applicant have "a cause of action enforceable by the Court, one in respect of which the Court then actually has jurisdiction".[113] In other words, where the defendant is outside the jurisdiction (which invariably would be the case under the present *Absconding Debtors Act*), the plaintiff must show that the case falls within Rule 25 of the Rules of Practice, the Rule governing service *ex juris*.[114] Although the grounds for service *ex juris*, particularly in the case of tort and contract claims, have been broadened significantly by recent amendments,[115] there may be some cases that do not come within Rule 25. In such a case, the creditor will not be able to attach his debtor's property. The use of provisional relief to secure jurisdiction is a subject to which we return later.[116]

On a number of occasions, the courts have considered whether resort may be had to absconding debtors legislation where the debtor does not reside or carry on business in the jurisdiction and the debt has not been contracted in the province, but the debtor has property in the jurisdiction.[117] In essence, the courts have said that the mere presence in the jurisdiction of property owned by the debtor is not a sufficient ground upon which to exercise *in personam* jurisdiction. Again, it is suggested that the courts have been concerned with the potential abuse that might result in cases where the debtor has had no connection with the jurisdiction.[118]

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[112] Manitoba Queen's Bench Rules, *supra*, note 89, r. 583(d).

[113] *Emperor of Russia v. Proskouriakoff* (1908), 8 W.L.R. 461, 18 Man. R. 56 (C.A.), at 72, *per* Perdue J.A.

[114] Rules of Practice, *supra*, note 15.

[115] *Ibid.*, r. 25(1)(*h*), as added by O. Reg. 106/75. See, for example, the following cases, all decided after r. 25(1)(*h*) was added in 1975: *John Ewing & Co. Ltd. v. Pullmax (Canada) Ltd.* (1976), 13 O.R. (2d) 587, 1 C.P.C. 251 (H.C.J.); *Can. General Electric Co. Ltd. v. C.M. Windows & Stained Glass Ltd.* (1977), 16 O.R. (2d) 188, 3 C.P.C. 298 (Master S.C.O.); *Skyrotors Ltd. v. Carriere Technical Industries Ltd.* (1979), 26 O.R. (2d) 207, 102 D.L.R. (3d) 323 (H.C.J.); *Vile v. Von Wendt* (1979), 26 O.R. (2d) 513, 103 D.L.R. (3d) 356 (Div. Ct.); and *Poirier v. Williston* (1980), 29 O.R. (2d) 303, 113 D.L.R. (3d) 252 (H.C.J.), aff'd (1981), 31 O.R. (2d) 320, 118 D.L.R. (3d) 576 (C.A.).

[116] See *infra*, sec. 7(d).

[117] See, for example, *Elgie v. Butt* (1899), 26 O.A.R. 13; *Cochran v. Duncan* (1841), 3 N.S.R. 80 (C.A.); *Mitcheson v. Duncan* (1842), 3 N.S.R. 86*n* (S.C.); and *Dudley v. Jones* (1876), 10 N.S.R. 306 (C.A.).

[118] Under the *Absconding Debtors Act*, *supra*, note 44, s. 2(1), of course, the absconding debtor must have been an Ontario resident. For a similar provision, see s. 2 of the now repealed *Absconding Debtors Act*, R.S.B.C. 1960, c. 1 (repealed by S.B.C. 1978, c. 11). No such requirement is to be found in the absconding debtors provisions of the

(4) *Corporate Debtors*

It should be noted that neither the *Absconding Debtors Act* nor the absconding debtors provisions of the *Small Claims Courts Act* would seem to distinguish between debtors who are natural persons and those who are corporate entities.[119] However, very few of the cases have been concerned with absconding corporate debtors.[120] Indeed, it is doubtful whether a corporation ever could be held to have departed from the jurisdiction with the requisite intent or to avoid being arrested or served with process. On the other hand, a corporate entity may come within the terms of section 159(*b*) of the *Small Claims Courts Act* by attempting to remove its assets from the jurisdiction.

(5) *Operation of Absconding Debtors Legislation*

In this section, we shall discuss briefly a number of issues related to the standard of proof required in applications for attachment. The approach of the courts to these issues has had an important practical impact on the efficacy of existing absconding debtors legislation.

In our discussion of the statutory scheme of Ontario's absconding debtors legislation, we made mention of the fact that an applicant for prejudgment attachment must file a supporting affidavit stating his cause of action.[121] While a creditor need not particularize his claim to the same extent as a statement of claim, he must establish a *prima facie* chance of success in the main action.[122] Similarly, although the issue of the debtor's liability to the applicant will not be determined upon an application for attachment,[123] the creditor's affidavit must disclose all the elements necessary for a finding that the debtor is liable to the creditor.[124]

The courts have taken a more stringent approach to some of the other matters that are required to be included in the material that must be filed in support of an application for attachment. For example, the courts have stated on a number of occasions that the creditor and other deponents

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Ontario *Small Claims Courts Act*, *supra*, note 45, and the earlier case law, therefore, may be applicable.

In some provinces, attachment has been made available in certain circumstances even though the debtor was not resident at the relevant time: see, for example, s. 4(1) of the *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2.

[119] Some legislation makes specific reference to corporate debtors: see, for example, r. 583(e), (f), and (g) of the Manitoba Queen's Bench Rules, *supra*, note 89.

[120] For a recent case concerning a corporate debtor and the problems that may arise when absconding debtors legislation is sought to be applied to such a debtor, see *Re Atlantic Pet Food Supply Inc.* (1977), 19 N.B.R. (2d) 602, at 608, 30 A.P.R. 602, at 608 (S.C., Q.B.), rev'd on other grounds (1978), 22 N.B.R. 81, 39 A.P.R. 81 (S.C., App. Div.).

[121] See *supra*, sec. 2(b)(i)b.

[122] See *Clish v. Baltimore-N.S. Mining Co.* (1906), 1 E.L.R. 235 (N.S.S.C.), at 236 ("it is sufficient if prima facie an interest in property is shewn").

[123] *Paulin v. Feinstein* (1918), 28 Man. R. 436 (C.A.).

[124] Accordingly, where the plaintiff fails to indicate that the contract in question has been executed by the defendant corporation, an attachment order should not issue: see *Gladwin v. Guildford* (1904), 40 N.S.R. 479 (S.C.). In other words, it is improper for the plaintiff to state a conclusion of law in his affidavit, without first deposing to the facts supporting the legal conclusion.

should state the grounds for their belief that the debtor has departed from the jurisdiction with the necessary intent.[125] In so holding, the courts have pointed to the potential harm that might befall a debtor against whom an attachment order is issued.[126]

The strict constructionist approach adopted generally by the courts to the prejudgment remedy of attachment is also evident from some of the grounds upon which attachment has been attacked successfully. Failure to state that the creditor's claim arose as a result of money lent *to the debtor*,[127] failure to include a statement that the debtor had property liable to seizure,[128] and failure to state that the debtor is justly and truly indebted to the creditor after making proper and just set-offs, allowances, and discounts (where so required by statute or the rules of procedure),[129] have all resulted in the setting aside of an attachment order. These examples are indicative of a judicial belief that the extraordinary and drastic remedy of attachment necessitates "that the requirements of the statutes or rules must be strictly complied with"[130] to entitle the plaintiff to such relief.

Insofar as proof that the debtor had the requisite intent when he left the jurisdiction is concerned, the courts have paid special attention to the circumstances surrounding the departure. Where the absence of the debtor is part of his normal routine, courts have been loath to hold that the debtor has departed with the necessary intent. If, on the other hand, the debtor's absence is unusual, a court will be much more likely to conclude that he has absconded. The above propositions may best be illustrated by a few decided cases.

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[125] *Canadian Bank of Commerce v. Kenzie*, [1923] 2 W.W.R. 993 (Sask. K.B.), and *Ex parte Moore; In re Long* (1883), 23 N.B.R. 229 (S.C.). See, also, *Bank of Upper Canada v. Spafford* (1832), 2 O.S. 373 (K.B.). Compare *Wakefield v. Bruce* (1869), 5 P.R. 77 (H.C.J.).

[126] See *Ex parte Moore; In re Long*, *supra*, note 125, at 240-41, *per* Wetmore J.:

> This is a very severe proceeding, and while a creditor's rights should be well cared for, debtors have some privileges which should be reasonably protected . . . .

We shall see a similar judicial attitude when we consider the remedy of prejudgment garnishment. Indeed, the courts may be even stricter in cases of prejudgment garnishment: see *infra*, sec. 2(b)(ii)d.

[127] *McKenzie v. Bussell* (1834), 3 O.S. 343 (K.B.).

[128] *Fitzgerald v. Warner* (1912), 7 D.L.R. 859, 2 W.W.R. 299 (Sask. Dist. Ct.). See *Absconding Debtors Act*, *supra*, note 44, s. 3(1), which requires the plaintiff to swear that the defendant at the time of his departure was "possessed to his own use and benefit of real or personal property in Ontario not exempt by law from seizure under execution".

[129] See *Keeler v. Hazlewood* (1883), 1 Man. R. 28 (Q.B.) and r. 583(d) of the present Manitoba Queen's Bench Rules, *supra*, note 89.

[130] *McKenzie v. Bussell*, *supra*, note 127, at 345, *per* Robinson C.J. Compare the statement of Macaulay J. in the same case at 346:

> The object of the present affidavit was not to arrest the person, but to attach the goods; there is therefore a difference, which may well be regarded upon applications of this kind. The strict rules laid down touching affidavits to hold to bail, are adopted in consequence of the loss of liberty . . . . That reason does not apply here; for although the object is two-fold – to secure the effects or enforce bail – still the defendant is not liable to arrest under the process, and need not enter bail unless desirous of appearing and contesting the claim.

In *Williams v. Sanford*,[131] for example, the debtor had left Nova Scotia to work in Massachusetts, as had been his custom. The Court concluded that the debtor's absence was for a temporary purpose only, not with the intent to defraud his creditors. In coming to this conclusion, the Court noted that the debtor's wife and child had remained in the jurisdiction during his absence,[132] and that the debtor had told the creditor that he was leaving.

In *Murdoch v. Hughes*,[133] even though the debtor was out of the jurisdiction for a longer period than normal, other evidence allowed the Court to determine that the absence was still only temporary and not with the intent to defraud his creditors. The Court pointed to the fact that the debtor had left his ongoing business in the hands of a clerk and that his prolonged absence was the result of the debtor being shipwrecked.

Evidence showing the debtor's intention to return to the jurisdiction and to maintain his domicile and residence prevented the Court in *Burt v. Burt*[134] from holding that the debtor had taken his leave with the requisite intent. In that case, the debtor had gone from Prince Edward Island to find work in New Brunswick. While in New Brunswick, he had joined the Canadian Merchant Marine.

Another factor that the courts have looked at to determine the question of intent is the debtor's dealings with his assets prior to his leave-taking. Where, for example, the debtor disposes of his property clandestinely, a court may be quite willing to draw the necessary inference of intent. If, on the other hand, the debtor sells his assets at a public auction that is openly advertised, a court may be hard pressed to make an adverse finding concerning the intent of the debtor.[135]

Before leaving the matter of proof of intent, one other point should be made. The courts have stated on a number of occasions that the mere nonpayment of a debt, or refusal to pay to a debt, by itself, will not support a finding that the debtor has departed from the jurisdiction intending to defraud his creditors.[136]

(6) *Setting Aside an Attachment Order*

Although the *Absconding Debtors Act* does not provide expressly for a right to challenge the validity of an attachment order,[137] undoubtedly the debtor himself may attack the order on the ground, for example, that it was made without jurisdiction because the debtor was not resident in Ontario prior to his departure. He may also seek to set aside the order where the plaintiff's affidavit is inadequate, or the necessary supporting material was not before the court at the time the plaintiff's application was considered.

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[131] (1911), 10 E.L.R. 151 (N.S. Co.Ct.).

[132] See, also, *Burt v. Burt* (1947), 21 M.P.R. 175 (P.E.I.S.C.).

[133] (1855), 2 N.S.R. 388 (C.A.).

[134] *Supra*, note 132. A brief absence of 5 days indicated an intention to return to the jurisdiction, not an intention to defeat one's creditors, in *Hewitt v. Gray* (1909), 7 E.L.R. 355 (P.E.I.S.C.).

[135] See *Hole v. Simpson* (1914), 6 W.W.R. 742 (Sask. S.C.), at 745, where the Court remarked: "Fraudulent or absconding debtors do not usually adopt this method of disposing of their goods or defrauding their creditors."

[136] See *Meadow Lake Car Sales Ltd. v. Michaud* (1978), 7 Alta. L.R. (2d) 289 (Alta. Dist. Ct.), citing *Canadian Bank of Commerce v. Kenzie*, *supra*, note 125, and *Lukian v. Shankoff*, *supra*, note 95.

A more difficult question concerns the right of a third party to attack an attachment order. For instance, the property attached may have been in the possession of a third party who claims that he is the owner of the property in question. In other words, can a person not a party to the cause of action upon which the attachment is based challenge the order?

In *Hart v. Cunningham*,[138] this question was raised squarely for the Court. Henry J. made the following remarks regarding collateral attacks on attachment proceedings:[139]

> [S]uch proceedings are, in their inception, *ex parte*, and for that reason their validity may be, and ought to be liable to be, impeached collaterally . . . . These latter cases establish the position that, where a judgment recovered contrary to law is prejudicial to the rights of a third party, he may avoid it collaterally.

Henry J. went on to say that collateral attack was not limited to the question whether the plaintiff's claim was "justly due" or whether the debt claimed was payable at the time the action was commenced.

Two decisions under the Saskatchewan *Absconding Debtors Act*[140] have also addressed the issue of collateral attack of an attachment order. McKay J.A., in *Coupal v. Buie*,[141] held that a third party claiming ownership of attached property could not set aside an attachment order on the basis of some "irregularity" in the proceedings taken to obtain the order. He suggested, however, that a third party might be able to impeach an order of attachment on the ground that the creditor has no reasonable cause of action against the debtor. This view of McKay J.A. was followed in the later decision of *Martin Ruby Ltd. v. National Upholstering Mfg. Co. Ltd.*[142] It should be noted that the Saskatchewan absconding debtors legislation at issue in these two cases specifically stated that a writ of attachment could be set aside by the court or a judge on satisfactory proof by affidavit that the creditor who sued out the writ had no reasonable cause for taking the proceeding.[143]

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[137] Compare Alberta Rules of Court, *supra*, note 89, r. 491; *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2, ss. 5 and 8; *The Judicature Act*, R.S.N. 1970, c. 187, ss. 82(3) and 90; Nova Scotia Rules, r. 49.10(2) and (3); Prince Edward Island Rules, r. 49.10(2), (3) and (4); *Code of Civil Procedure*, R.S.Q. 1977, c. C-25, art. 738; and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 11.

[138] (1898), 40 N.S.R. 229 (S.C.). See, also, *Gormley v. DeBlois* (1912), 8 D.L.R. 109, 46 N.S.R. 280 (S.C.).

[139] *Ibid.*, at 230.

[140] See now R.S.S. 1978, c. A-2.

[141] [1926] 2 D.L.R. 918, [1926] 2 W.W.R. 242 (Sask. C.A.).

[142] (1964), 47 W.W.R. 211 (Sask. Dist. Ct.).

Some legislation authorizing attachment of the debtor's property provides expressly for the time within which the defendant or other person may challenge the validity of the attachment order.[144] However, where the legislation is silent on this matter, it would seem that the court considering the impeachment motion may have regard to the lapse of time since the making of the order, especially where the motion to impeach the attachment order is based on some irregularity in the procedure.[145]

Another question that has arisen in respect of the power of the court to set aside an attachment order concerns the authority of the court to impose terms upon the defendant as a condition of setting aside the order. In *Wilson v. Smith*,[146] the Manitoba Court of Queen's Bench concluded that, "where the defendant comes to the Court *ex debito justitiae* [as a matter of right], terms cannot be imposed without his consent, although he may be deprived of his costs if he does not consent".[147] Therefore, although the court in such circumstances cannot make its order to set aside an attachment order that has been irregularly obtained conditional upon the defendant's undertaking not to seek damages for wrongful attachment, the court may refuse to award costs against the creditor (or sheriff) unless the debtor gives such an undertaking.

(7) *Liability for Wrongful Attachment*

Turning to the question of the creditor's liability for wrongful attachment, it would appear that an attaching creditor will be protected from an action in trespass as long as the "writ of attachment has *prima facie* been properly issued on statutory grounds without malice and with reasonable and probable cause", even though subsequently it is set aside upon proof that such grounds did not exist.[148] Otherwise, "it would be extremely hazardous for any creditor to resort to attachment proceedings to recover a just debt":[149] to avoid liability the creditor would have to have "absolute and indefensible proof of the act and intent of the debtor".[150] It may be argued that, since prejudgment attachment is "usually invoked in an emergency suddenly disclosed and upon information received from sources other than the debtor himself",[151] the object of the remedy would be frustrated by any such strict requirement.

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[143] See now *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 11.

[144] See, for example, *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2, s. 8 (within 60 days of the publication in The Royal Gazette of the prescribed notice).

[145] *McPherson v. Patmore* (1964), 49 W.W.R. 567 (B.C.C.A.).

[146] (1893), 9 Man. R. 318 (Q.B.).

[147] *Ibid.*, at 321, *per* Taylor C.J.

[148] See *Thomson v. Whitman*, [1924] 2 D.L.R. 1012, [1924] 2 W.W.R. 89 (Man. K.B.), at 92, *per* Curran J.

[149] *Ibid.*

[150] *Ibid.*

[151] *Ibid.*

The sheriff would seem to be protected from liability by the attachment order where the property seized is in the possession of the debtor.[152]

(ii) Prejudgment Garnishment

a. *Introduction*

As was mentioned earlier,[153] until recently a small claims court creditor could have resort to two prejudgment remedies against his debtor's property: attachment of an absconding debtor's personal estate and effects, and prejudgment garnishment of any debts owing to his debtor by third persons. However, in 1977, some 100 years after its introduction,[154] prejudgment garnishment in the small claims courts was abolished.[155] In spite of the fact that the *Wages Act*[156] expressly prohibits the prejudgment garnishment of wages, this remedy was thought to be objectionable because of its possible use as a means of intimidating debtors – by garnishing money in the debtor's bank account, for example – forcing them to pay the amount claimed by their creditors, whether owing or not.[157]

b. *The Statutory Scheme*

From 1869, when prejudgment garnishment first was introduced in Ontario, until its repeal in 1977, the grounds and the procedure for such relief changed very little. Section 151(1) of *The Small Claims Courts Act* provided as follows:

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[152] *Mills v. McLean* (1876), 10 N.S.R. 379 (S.C.). The subject of sheriff's liability is discussed in Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

[153] *Supra*, sec. 2(b).

[154] *An Act to amend the Acts respecting Division Courts*, 32 Vict., c. 23.

[155] *The Small Claims Courts Amendment Act, 1977*, S.O. 1977, c. 52, s. 16.

[156] See now R.S.O. 1980, c. 526, s. 9, which reads as follows:

> 9. Proceedings to attach any debt due or accruing due to any mechanic, workman, servant, clerk or employee for or in respect of his wages shall be taken only where the claim of the creditor against the debtor is upon a judgment.

[157] During the legislative debates for the abolition of prejudgment garnishment in the small claims courts, Patrick Lawlor, M.P.P., remarked as follows:

> Up until this time in history, one of the most iniquitous procedures embodied in that particular piece of legislation, which is nowhere else in the law, it is unheard of, is that you can go and garnishee a man's salary or you can garnishee his bank account or you can seize any money that you happen to know the whereabouts of, even if it's under the bed, without issuing a writ, without having made an adjudication of the legitimacy of the debt itself as to the merits of it, whether it is really owing, whether there's a defence, whether it is only partially owing or what not. You get hit right between the eyes and do they ever take advantage of it.
>
> The legislation being brought before us is saying, 'That piece of iniquity is going to be knocked out. If you want your garnishments, you are going to get them after you have legitimized them, after you have proven that the money is really owing.'
>
> Why the old legislation has existed so long I don't know. Certainly the complaint has been raised a number of times in this House and very often comes into our constituency office. A man very often loses his job because of it.

See *Legislature of Ontario Debates*, 31st Parl. 1st Sess., November 7, 1977, at 1641.

> 151.-(1) Where a judgment has not been recovered, a plaintiff in an action in which a debt or money demand summons[158] may be issued may cause to be issued out of the court of the division in which the garnishees, or one of them, if they are joint garnishees, reside or carry on business, a garnishment summons with the particulars of his claim against the defendant with reasonable certainty and detail attached thereto or endorsed thereon.

A garnishment summons served as both the originating process *vis-à-vis* the debtor[159] and as a direction to garnish *vis-à-vis* the garnishee and the debtor.[160] It was available only where a debt was claimed or a money demand summons could be employed. A creditor employing this garnishment summons procedure could apply for judgment against a garnishee, and if the garnishee failed to pay the amount of the debt into court, execution could issue against him.

At this juncture, it may be appropriate to compare the prejudgment remedies of garnishment and attachment. First, it is important to note that prejudgment garnishment was available under *The Small Claims Courts Act* without proof that the debtor had taken steps to defeat his creditors. No allegation that the debtor had departed the jurisdiction with intent to defraud his creditors or to avoid arrest or service of process was necessary. No affidavit in support of a request for a garnishment summons was necessary. The debtor's main safeguard against abuse of the remedy of prejudgment garnishment was its restriction to debt and money demand claims. This controlling feature is similar to the limitation of prejudgment attachment under Ontario's absconding debtors legislation to claims of indebtedness. We shall consider further this aspect of prejudgment garnishment below.[161] However, before we do so, a brief survey of the availability of prejudgment garnishment in some of the other provinces may be useful.

c. *Prejudgment Garnishment: A Canadian Survey*

Ontario certainly was not alone in permitting prejudgment garnishment. Indeed, many of the provinces continue to allow a creditor to garnish debts owing to a debtor by third persons prior to securing a judgment against the debtor. Moreover, where prejudgment garnishment is available, it is generally available to all creditors, and is not restricted to creditors in the small claims courts or their equivalent.

(1) *Alberta*

The Alberta Rules of Court provide that, in any action for a debt or liquidated demand, upon affidavit by the plaintiff, his solicitor, or agent, the court upon an *ex parte* application may allow the plaintiff to issue a garnishee summons before judgment.[162] The affidavit of the plaintiff, his solicitor, or agent must (1) swear positively to the facts establishing the cause of action; (2) state a belief that the plaintiff is entitled to the relief claimed; (3) exhibit an understanding that, if moneys are paid into court under a garnishee summons, the plaintiff will proceed with the action without delay; and (4) establish a reasonable possibility that the plaintiff will be unable to collect all or part of his claim or be subjected to unreasonable delay in the collection of the claim unless a garnishee summons is issued.[163] In all other respects, the procedure is identical to that which must be followed when garnishment after judgment is desired.

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[158] See *The Small Claims Courts Act*, R.S.O. 1970, c. 439, ss. 88-90.

[159] *Ibid.*, s. 151(2).

[160] *Ibid.*, s. 153. The Act also contained provisions to allow a garnishee to dispute a garnishment summons, and other interested persons to assert a claim to the debt in question: see ss. 154(2) and 155, respectively.

[161] See *infra*, sec. 2(b)(ii)d.(2).

[162] Alberta Rules of Court, *supra*, note 89, r. 470(1).

A few features of Alberta's prejudgment garnishment remedy are worth noting. First, this enforcement device is available only where the enforcement of the plaintiff's judgment may be subject to reasonable doubt. In this respect, the remedy is similar to attachment under absconding debtors legislation, since the remedy may be employed only where the debtor has taken steps to thwart collection of the creditor's claim.

Secondly, the material that must be filed in support of an application for a garnishee summons before judgment is similar to that required under Ontario's absconding debtors legislation.[164] It will be remembered that, under the prejudgment garnishment provisions of *The Small Claims Courts Act*, no supporting affidavit had to be filed. Thirdly, a creditor resorting to prejudgment garnishment under the Alberta Rules of Court must undertake to proceed without delay in the prosecution of his action against the debtor.[165]

Finally, it should be noted that garnishment before judgment is available under the Alberta Rules of Court only in respect of a claim for a debt or liquidated demand. As we shall see, the phrase "debt or liquidated demand", like the phrase "debt or money demand" found in former section 151(1) of *The Small Claims Courts Act*, has given rise to real legal difficulties.

(2) *British Columbia*

Prejudgment garnishment is authorized by section 4 of the British Columbia *Court Order Enforcement Act*.[166] Where a creditor has commenced an action against a debtor, in order to obtain a garnishing order before judgment, the creditor, his solicitor, or some other person aware of the facts must swear an affidavit stating "(i) that an action is pending; (ii) the time of its commencement; (iii) the nature of the cause of action; (iv) the actual amount of the debt, claim or demand; and (v) that it is justly due and owing, after making all just discounts".[167] The affidavit must also indicate that some person is "indebted or liable to the defendant", and "is in the jurisdiction of the court", stating, "with reasonable certainty, the place of residence of the garnishee".[168] By virtue of section 4(2) of the *Court Order Enforcement Act*, a garnishing order may be obtained even before an action has been commenced.

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[163] *Ibid.*

[164] See discussion *infra*, sec. 2(b)(ii)d.(3).

[165] Compare s. 18 of Ontario's *Absconding Debtors Act*, *supra*, note 44, which provides that an order of attachment will bind the debtor's property only for a period of three months, unless an execution is filed by some creditor within three months of the issuance of the attachment order.

[166] R.S.B.C. 1979, c. 75.

[167] *Ibid.*, s. 4(1)(d).

Unlike the prejudgment garnishment provisions of the Alberta Rules of Court, under the British Columbia *Court Order Enforcement Act* prejudgment garnishment will be available if there is a debt, claim, or demand that is justly due and owing "after making all just discounts", such as by right of set-off. Also in contrast to the Alberta provisions, a creditor relying on section 4 of the *Court Order Enforcement Act* need not state that collection of his debt, claim, or demand may be defeated unless a garnishing order before judgment is granted. One final point about the British Columbia prejudgment garnishment legislation should be made. This remedy may not be used to garnish salary or wages.[169]

(3) *Manitoba*

The Manitoba *Garnishment Act*[170] also authorizes garnishment before judgment. The circumstances in which this remedy is available and the procedure to be followed are dealt with by the Manitoba Queen's Bench Rules.

Prejudgment garnishment may be requested under these Rules where the creditor's claim is in respect of a debt or liquidated demand in money arising

> (i) on a contract, express or implied (e.g., on a bill of exchange, promissory note, cheque, order, account, or other simple contract); or
>
> (ii) on a bond or contract under seal for payment of a liquidated sum; or
>
> (iii) on a judgment; or
>
> (iv) by a statute; or
>
> (v) on a guaranty, whether under seal or not, where the claim against the principal is in respect of a debt or liquidated demand; or
>
> (vi) on a trust; . . .[171]

Pursuant to Rule 526(1)(c), the applicant must file an affidavit in support of his application stating "that an action is pending and the time of its commencement, the nature of the cause of action, the amount of the claim and that the same is justly due and owing to the [creditor] by the [debtor]". Section 12 of *The Garnishment Act* prohibits the prejudgment garnishment of wages.[172]

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[168] *Ibid.*

[169] *Ibid.*, s. 4(3).

[170] R.S.M. 1970, c. G20, s. 5.

[171] See rr. 524 and 34 of the Manitoba Queen's Bench Rules, *supra*, note 89.

(4) *Prince Edward Island*

Section 5 of the *Garnishee Act*[173] of Prince Edward Island states as follows:

> 5.-(1) Any debts or liabilities due or owing or accruing due by any garnishee to any judgment debtor, or to any defendant or primary debtor, may be attached in the Supreme Court in the manner and with the effect prescribed by the rules of the court.
>
> (2) The Rules of the Supreme Court, as set forth in the Schedule, or as hereafter amended according to law, shall be read and construed as forming a part of this Act.

It would appear, however, that wages or salary cannot be garnished before judgment.[174]

The applicable procedure may be found in the Prince Edward Island Rules. Rule 49.14(a) stipulates that, where a judgment has not been recovered, the plaintiff, his attorney, or some other person aware of the facts, must state in an affidavit "the nature of the cause of the action and the actual amount of the debt, claim or demand, and that the same is justly due and owing to the plaintiff by the defendant after making all just discounts". As is the case under the British Columbia *Court Order Enforcement Act*,[175] Rule 49.14(c) of the Prince Edward Island Rules permits garnishment prior to judgment both before and after the commencement of an action against the debtor. However, Rule 49.14(c) of the Prince Edward Island Rules does require the creditor to commence his action within ten days of the service of the order upon the garnishee, and to proceed with the action without delay. Failure to do so may result in discharge of the garnishment order.[176]

(5) *Saskatchewan*

Pursuant to section 3(1) of the Saskatchewan *Attachment of Debts*

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[172] Added to *The Garnishment Act*, *supra*, note 170, by S.M. 1970, c. 18, s. 6.

[173] R.S.P.E.I. 1974, c. G-2.

[174] *Ibid.*, s. 17.

[175] *Supra*, note 166.

[176] Rule 49.14(c) of the Prince Edward Island Rules states: ". . . if the creditor does not so proceed or commence his action, the debtor may issue a summons calling on the creditor to show cause why the attaching order should not be discharged, and upon the return of the summons the court or a judge may make whatever order the justice of the case may require, and the costs shall be in the discretion of the court or judge".

Act,[177] "a plaintiff in an action for debt or liquidated demand may issue a garnishee summons". Again, the creditor, his solicitor, or agent must file a supporting affidavit setting out the nature and amount of the creditor's claim and swearing positively to the indebtedness of the debtor.[178] This affidavit also must include a statement to the effect that "to the best of the deponent's information and belief, the proposed garnishee . . . is indebted to the defendant".[179] The Saskatchewan Act expressly permits the prejudgment garnishment of a debtor's wages or salary.[180]

d. The Jurisprudence

The succeeding analysis is similar to that adopted earlier in respect of attachment under Ontario's absconding debtors legislation.[181]

(1) *General Considerations*

The courts, perhaps even more so than with respect to the prejudgment remedy of attachment, have adopted a strict constructionist approach to prejudgment garnishment legislation. As in the case of prejudgment attachment, the courts have been conscious of the fact "that garnishee proceedings before judgment are foreign to common law".[182] Similarly, the courts have viewed prejudgment garnishment as an extraordinary remedy[183] that could give rise to great hardship[184] and, consequently, have demanded strict compliance with,[185] or meticulous observation of,[186] the statutory or regulatory requirements to secure this remedy. This approach was evident in the early case law[187] and continues to guide the courts today.[188] It is a philosophy that has found judicial favour in almost every province that permits a creditor to garnish debts owed to his debtor before judgment.[189] Perhaps the most succinct statement of the judicial position respecting prejudgment garnishment is to be found in the Alberta case of *MacFarlane v. Owen*,[190] where Winter D.C.J. stated as follows:[191]

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[177] *The Attachment of Debts Act*, R.S.S. 1978, c. A-32.

[178] *Ibid.*, s. 3(2)(*a*).

[179] *Ibid.*, s. 3(2)(*b*).

[180] *Ibid.*, s. 9.

[181] See *supra*, sec. 2(b)(i)c.

[182] See *Erwin W. Block Professional Corp. v. Dickson* (1979), 9 Alta. L.R. (2d) 322 (S.C., T.D.), at 324, *per* Decore L.J.S.C.

[183] *Mumford Medland Ltd. v. Certified Concrete (Central) Ltd.* (1967), 59 W.W.R. 378 (Sask. C.A.); *Joncas v. Plotkins*, [1934] 3 D.L.R. 799, [1934] 2 W.W.R. 142 (Alta. S.C., T.D.); *McParland v. Seymour*, [1925] 4 D.L.R. 944, [1925] 3 W.W.R. 666 (Alta. S.C., App. Div.); *Cascade Builders Ltd. v. Benjamin Excavating Ltd.*, [1971] 1 W.W.R. 700 (Alta. S.C., T.D.); *Erwin W. Block Professional Corp. v. Dickson*, *supra*, note 182; *Halpin v. Acceptance Mortgage Corp. Ltd.* (1966), 55 W.W.R. 636 (B.C.S.C.) ("extraordinary form of relief"); *Knowles v. Peter* (1954), 12 W.W.R. 560 (B.C.S.C.) ("extraordinary process"); *Medpak Ltd. v. Matz*, [1979] 1 W.W.R. 1, 8 C.P.C. 314 (Man. Q.B.); and *Avco Finance Ltd. v. Suppa* (1967), 62 W.W.R. 124 (N.W.T. Terr. Ct.).

[184] See, for example, *Ridgeway Pacific Const. Ltd. v. United Contractors Ltd.*, [1974] 6 W.W.R. 662 (B.C.S.C.), at 667, *per* Meredith J.:

> I recognize that in all probability freezing a substantial sum of the defendant's money, if the defendant is found ultimately not liable for payment, works a regrettable hardship on the defendant, indeed a hardship which could in some circumstances be disastrous.

Reversed on appeal [1976] 1 W.W.R. 285 (B.C.C.A.). See, also, *Page v. Brown* (1978), 22 Nfld. & P.E.I.R. 497, at 503, 58 A.P.R. 497, at 503 (P.E.I.S.C.), *per* C.R. McQuaid J.

[185] *Joncas v. Plotkins*, *supra*, note 183; *Banque Canadienne Nationale v. Labine*, [1933] 2 D.L.R. 432, [1933] 1 W.W.R. 385 (Alta. S.C., App. Div.); *McParland v. Seymour*, *supra*, note 183; *Boake Realty Ltd. v. Macklin* (1968), 67 W.W.R. 113 (Alta. Dist. Ct.); *Erwin W. Block Professional Corp. v. Dickson*, *supra*, note 182; *Halpin v. Acceptance Mortgage Corp. Ltd.*, *supra*, note 183; and *Richardson v. Roberts* (1909), 10 W.L.R. 497 (Sask. Local Master).

> The remedy of attaching funds of a defendant before judgment by obtaining garnishee summons is an extraordinary remedy although one in very common use. It is very frequently the cause of great hardship, and even injustice to a defendant and all the requirements of the rules in relation thereto must be rigidly carried out if the plaintiff desires to obtain the advantage of the proceeding.

The result of this judicial posture toward prejudgment garnishment has been a very technical application of statutory and regulatory provisions concerning this "extraordinary remedy".

(2) *Nature of the Plaintiff's Claim*

Reference already has been made to the fact that prejudgment garnishment under the Ontario *Small Claims Courts Act* was restricted to cases concerning "a debt or money demand". The phrase "debt or liquidated demand" or "debt, claim or demand" appears in other jurisdictions as well.[192] However, no matter what terminology has been employed, substantial litigation has resulted, affording little practical guidance. A brief look at some of the case law should prove the point.

Davies, the author of *McKeon's Small Claims Court Handbook*,[193] makes the following comments respecting the meaning of the phrase "debt or money demand":[194]

> A debt has been defined as that for which an action for debt will lie – a sum of money due by express and certain agreement. *N.H. Saw Mill Co. v. Fowler* (1859), 28 Con. 108. A money demand is one arising out of a contract, express or implied, which from its nature enables the plaintiff to make an affi-

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[186] *Mumford Medland Ltd. v. Certified Concrete (Central) Ltd.*, *supra*, note 183; *Knowles v. Peter*, *supra*, note 183.

[187] See, for example, *Whittimore v. Herbert* (1878), 18 N.B.R. 361 (S.C.), and *Nagengast v. Miller* (1885), 3 Man. R. 241 (Q.B.).

[188] See, for example, *Erwin W. Block Professional Corp. v. Dickson*, *supra*, note 182; *Medpak Ltd. v. Matz*, *supra*, note 183; and *Page v. Brown*, *supra*, note 184.

[189] See the cases cited *supra*, notes 183-88.

[190] [1917] 3 W.W.R. 371 (Alta. Dist. Ct.).

[191] *Ibid.*, at 372.

[192] See discussion *supra*, sec. 2(b)(ii)c.

[193] Davies, *McKeon's Small Claims Court Handbook* (3d ed., 1975).

[194] *Ibid.*, at 66.

> davit that the sum sued for is actually due. *Mills v. Long* (1877), 58 Ala. 458. The words used in this section include any claim, legal or equitable, on contract, express or implied, or under a statute, on which a certain sum of money, not being unliquidated damages, is due and payable, though an enquiry may be necessary to ascertain the exact amount due. *Re Mager v. Can. Tin Plate Dec. Co.* (1903), 7 O.L.R. 25; *McIntyre v. Munn* (1903), 6 O.L.R. 290. See *R. 33* and Holmested & Gale, p. 585.

What is of particular interest in Davies' remarks is his reference to Rule 33 of the Supreme Court of Ontario Rules of Practice,[195] which allows a person to commence an action by way of a specially endorsed writ where, *inter alia*, the claim is in respect of "a debt or liquidated demand in money". However, this phrase continues to give rise to difficulty in application,[196] and a recent spate of decisions has not advanced the matter greatly.[197]

Unfortunately, case law in the other provinces where the phrase "debt or liquidated demand" is used, far from being of assistance, may give rise to even greater difficulty. For example, the leading authority respecting the meaning of the phrase "debt or liquidated demand", found in section 3(1) of the Saskatchewan *Attachment of Debts Act*,[198] is *Alm v. Tyrone Hotels (Sask.) Ltd.*,[199] where Mr. Justice Doiron adopted the following definition:[200]

> 'Perhaps the best statement which can be attempted of the meaning of the expression "debt or liquidated demand (in money)", as used in 1851, is that it covered any claim:
>
> '(a) for which the action of debt would lie; (b) for which an indebitatus (or "common") count would lie – including those cases formerly covered by the *quantum meruit* or *quantum valebat* counts, notwithstanding that the only agreement implied between the parties in such cases was for payment at a "reasonable" rate; (c) for which covenant, or special *assumpsit*, would lie, provided that the claim was for a specific amount, not involving in the calculation thereof elements the selection whereof was dependent on the opinion of a jury.'

In *McMeekin v. Certified Concrete (Central) Ltd.*,[201] the Court also referred to the old count of *indebitatus*. It would appear that the forms of action of pre-*Judicature Act* days continue to govern, in this area of Saskatchewan law at least.[202] Case law in Alberta,[203] British Columbia,[204] and Prince Edward Island[205] follows either the Saskatchewan or Ontario approach, regardless of whether the phrase "debt or liquidated demand" or "debt, claim or demand" is used in the rules or statute.

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[195] *Supra*, note 15.

[196] For a collection of relevant cases, see Hemmerick (ed.), *Holmested and Gale on the Judicature Act of Ontario and the Rules of Practice* (1982).

[197] See, for example, *Kennedy v. 315812 Ont. Ltd.* (1976), 2 C.P.C. 281 (Ont. H.C.J.); *Rasins v. Place Park (Windsor) Ltd.* (1977), 4 C.P.C. 63 (Master S.C.O.); *High Point Mngt. Services Ltd. v. Royal Bengal Restaurant Ltd.* (1978), 19 O.R. (2d) 133, 6 C.P.C. 263 (Master S.C.O.); and *Hammond v. Parsons* (1978), 19 O.R. (2d) 162 (Master S.C.O.).

[198] *Supra*, note 177.

[199] (1963), 42 W.W.R. 297 (Sask. Q.B.).

[200] *Ibid.*, at 301.

[201] (1966), 58 W.W.R. 56 (Sask. Q.B.). While a claim for *quantum meruit* would seem to fall within the meaning of "debt or liquidated demand" as interpreted in *Alm* and *McMeekin*, the Court in *Wright v. Galisheff*, [1948] 1 W.W.R. 1082 (Sask. Dist. Ct.) came to a different conclusion. The Court in this case adopted an approach to the scope of the term "liquidated demand" similar to that exhibited in the Ontario cases, *supra*, note 197.

(3) *Operation of Prejudgment Garnishment Legislation*

As in the case of our discussion of attachment, we shall examine in this section some of the more frequently litigated issues concerning prejudgment garnishment, such as the standard of proof and the need for particularization. The impact of the judiciary's strict constructionist approach should be evident from the ensuing discussion.

Section 151(1) of *The Small Claims Courts Act* did not require a creditor seeking prejudgment garnishment to file an affidavit in support of his request. However, in those provinces where a supporting affidavit is required, there has been some controversy about the persons who may furnish the necessary affidavit. For example, in spite of the fact that the Alberta enabling legislation allows the necessary affidavit to be sworn by the creditor, his solicitor, or agent,[206] it has been held that the affidavit of an articled student will not suffice.[207] In a more recent case,[208] the British Columbia Supreme Court concluded that an articled student's affidavit was sufficient under that Province's legislation, since it specifically stated that the affidavit could be sworn by any person "aware of the facts".[209]

One other point regarding the question of who may swear the supporting affidavit should be made. In at least two cases,[210] the court has set aside a prejudgment garnishment order on the ground that the deponent had failed to state the capacity in which the affidavit was sworn.

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[202] For a detailed analysis of the prejudgment garnishment provisions of *The Attachment of Debts Act*, see Selnes, "Pre-judgment Garnishment Proceedings" (1977-78), 42 Sask. L. Rev. 119.

[203] See *Connors v. Egli*, [1923] 4 D.L.R. 1199, [1923] 3 W.W.R. 999 (Alta. S.C., T.D.); *Halifax Fire Ins. Co. v. McGilvray*, [1940] 1 D.L.R. 77, [1939] 3 W.W.R. 542 (Alta. S.C., T.D.); *Van Ripper v. Bretall* (1913), 13 D.L.R. 352, 4 W.W.R. 1289 (Alta. S.C., T.D.); and *International Supply Co. Ltd. v. Black Diamond Oil Fields Ltd.* (1915), 8 W.W.R. 475 (Alta. S.C., T.D.).

[204] See *Pe Ben Industries Co. Ltd. v. Chinook Construction & Engineering Ltd.*, [1977] 3 W.W.R. 481 (B.C.C.A.), and *Lennox v. Pacific Coast Condominium* (1977), 4 B.C.L.R. 242 (S.C.).

[205] See *Page v. Brown*, *supra*, note 184 (P.E.I.S.C.) (unliquidated damages do not constitute "a debt, claim or demand"). Compare *Huhn v. Bogach*, [1928] 3 W.W.R. 422 (Man. Co. Ct.).

[206] See discussion *supra*, sec. 2(b)(ii)c.(1).

[207] See *Mohr v. Parks* (1910), 15 W.L.R. 250, 3 Alta. L.R. 252 (S.C. en banc).

[208] *Couston v. Couston* (1952), 7 W.W.R. 621 (B.C.S.C.).

[209] See *Court Order Enforcement Act*, R.S.B.C. 1979, c. 75, s. 4(1).

[210] *Imperial Bank of Canada v. Miller* (1910), 13 W.L.R. 260 (Sask. Dist. Ct.), and *McGillivray v. Beamish* (1915), 23 D.L.R. 324, 7 W.W.R. 1188 (Sask. S.C.). In *Hart v. Greer (No. 2)* (1915), 9 W.W.R. 709 (Sask. Dist. Ct.), the Court held that failure to state on whose behalf the affidavit had been made was "a mere irregularity curable by amendment".

The courts have also been consistent in demanding strict compliance with other statutory requirements respecting the affidavit that, in most jurisdictions, must be filed in support of a request for prejudgment garnishment. Prejudgment garnishment orders have been set aside on the following grounds of non-compliance: the affidavit was sworn prior to the commencement of the main action;[211] the affidavit failed to state that the garnishee was within the court's jurisdiction;[212] the affidavit did not include a statement that the sum claimed was "justly due and owing"[213] after making "all just discounts";[214] and the affidavit did not indicate that there was a reasonable possibility that collection of the creditor's claim would be defeated or delayed without the relief requested.[215] Another ground upon which the courts have fastened to set aside prejudgment garnishment orders is inadequate particularization of the creditor's claim. Ontario's *Small Claims Courts Act* required that the garnishee summons describe the creditor's claim "with reasonable certainty and detail".[216] Much of the legislation in the other jurisdictions that we examined speaks in terms of a requirement to state the "nature of the cause of action".[217]

There would appear to be some difference of opinion respecting the purpose of the particularization requirement. On the one hand, some courts have suggested that the reason that the creditor is required to state his claim with sufficient particularity is to enable the defendant and the garnishee to know "precisely what is occurring so that they may act appropriately".[218] On the other hand, it has been argued that stating the nature of the creditor's claim "is not to warn the defendant of the grounds of the plaintiff's cause of action, for these are revealed in the endorsement on the writ . . . . The judge however must be satisfied that the cause of action is such a one as comes within the terms of the Act . . . ."[219] While the cases reflect both points of view, the statements in the cases generally would seem to favour the latter opinion.[220]

Whatever the purpose of the requirement of particularization, it is clear from the case law that courts are more than willing to exercise their discretion to set aside prejudgment garnishment orders for failure to meet this requirement. Accordingly, courts have set aside a prejudgment garnishment order where the statement of the nature of the creditor's claim was insufficient to allow the court to say that the claim was a liquidated demand,[221] where the affidavit failed to state all the elements of the cause of action,[222] and where the claim was too generally stated.[223] Mere reference in the supporting affidavit to the statement of claim in the main action will not be sufficient to satisfy the requirement of particularization.[224] However, annexing the statement of claim as an exhibit to the supporting affidavit may be sufficient.[225] The above discussion is not to suggest, however, that the affidavit supporting an application for garnishment before judgment need be of such a character "as would establish all that must be proved when the case comes to trial".[226] Rather, it would appear that, as in the case of attachment, the affidavit need establish only a *prima facie* chance of success in the main action.

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[211] See, for example, *McParland v. Seymour*, *supra*, note 183, and *Erwin W. Block Professional Corp. v. Dickson*, *supra*, note 182. Compare *Stewart & Matthews Co. v. Ross* (1912), 7 D.L.R. 378, 17 W.L.R. 179 (Sask. S.C.).

[212] *Nagengast v. Miller*, *supra*, note 187, and *Hamilton v. McDonald* (1885), 2 Man. R. 114 (C.A.). Compare *Wilson v. Douglas*, [1931] 2 D.L.R. 413, 3 M.P.R. 84 (N.B.S.C., App.Div.) (a postjudgment garnishment case).

[213] *Haug v. Brown*, [1934] 2 D.L.R. 302, [1934] 1 W.W.R. 183 (Man. C.A.), and *McDonald v. Yanchuk*, [1941] 4 D.L.R. 350, [1941] 2 W.W.R. 474 (B.C.S.C.).

[214] *Nagengast v. Miller*, *supra*, note 187.

[215] *Cascade Builders Ltd. v. Benjamin Excavating Ltd.*, *supra*, note 183.

[216] *The Small Claims Courts Act*, *supra*, note 46, s. 151(1).

[217] See discussion *supra*, sec. 2(b)(ii)c.

[218] See, for example, *Garon Realty & Ins. Ltd. v. James* [1977] 1 W.W.R. 45, at 48, 8 C.P.C. 65 (B.C.S.C.), *per* Lander L.J.S.C.

[219] *Hall v. Nutria Inc.* (1958), 24 W.W.R. 479 (B.C.S.C.), at 480, *per* Ruttan J.

[220] See *Salander v. Jensen* (1907), 6 W.L.R. 401 (Y.T.C.A.), and *Vickery v. Security Home Financing Ltd.* (1977), 6 C.P.C. 169 (B.C.S.C.). Compare *Thomee v. Westcott* (1922), 66 D.L.R. 250, [1922] 2 W.W.R. 727, (Alta. S.C., App. Div.), at 732, where the Court concluded that the purpose of the Alberta rule was to protect debtors from "mere shots in the dark and from being bothered by garnishee summonses being served upon them recklessly and without any reason whatever". In other words, the requirement of particularity enabled the courts to act as a screening device.

Regarding the form of the supporting affidavit, here too the courts have sought to provide debtors with some added protection against the rigours of prejudgment garnishment. For example, a question has arisen whether such affidavits must be restricted to the statement of facts within the knowledge of the deponent or whether they may be based on information and belief. Some legislation makes specific reference to the information and belief of the deponent. For instance, the Saskatchewan *Attachment of Debts Act*[227] requires the deponent to state in his affidavit that, "to the best of [his] information and belief, the proposed garnishee

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[221] See, for example, *Alta. Tractor Parts Ltd. v. Czech Constr. Ltd.* (1959), 30 W.W.R. 163 (Alta. S.C., T.D.); *Smith v. Metzer* (1915), 7 W.W.R. 1386 (Alta. S.C.); and *A.H. McLeod & Son Ltd. v. Hudson Hope Holdings Ltd.* (1964), 49 W.W.R. 422 (B.C.S.C.).

[222] See, for example, *E.A. Aim Ltd. v. Kost* (1957), 21 W.W.R. 480 (B.C.S.C.), and *McMeekin v. Certified Concrete (Central) Ltd.* (1966), 58 W.W.R. 56 (Sask. Q.B.) (failure to allege proper contract for claim based on *quantum meruit*).

[223] *Chauvel v. Chauvel* (1964), 47 W.W.R. 574 (B.C.S.C.). In this case, the plaintiff sought the return of certain moneys held in trust for him by the defendant. The Court granted the defendant's application to have the garnishment order set aside, commenting as follows (at 576):

> The nature of the alleged trust is not described, nor is it stated whether the trust arises under a will or under an agreement expressed or implied or a resulting trust and no breach of an undescribed trust is alleged.

See, also, *Joncas v. Plotkins*, *supra*, note 183 (no indication of the basis upon which plaintiff claimed defendant indebted to him), and *Mumford Medland Ltd. v. Certified Concrete (Central) Ltd.* (1977), 6 C.P.C. 169 (B.C.S.C.) (plaintiff's claim for commission and *quantum meruit*, but affidavit failed to state facts concerning the oral agreement between the parties and the rate of pay).

[224] *Giffen v. Lavin*, [1919] 2 W.W.R. 491 (Alta. S.C., T.D.); *Scott v. Chase Creek Lumber Co. Ltd.*, [1921] 2 W.W.R. 773 (Alta. S.C.); and *U.S.A. v. Annesley* (1957), 21 W.W.R. 520 (B.C.S.C.). Compare *Beaubier v. Lloyd* (1918), 39 D.L.R. 439, [1918] 1 W.W.R. 772 (Alta. S.C., App. Div.), *per* Beck J., dissenting.

[225] *Clokey v. Huffman* (1912), 1 D.L.R. 679, 1 W.W.R. 1093 (Sask. S.C.).

[226] *Pomfret v. Morie*, [1931] 3 D.L.R. 557, at 560, [1931] 2 W.W.R. 477 (Alta. S.C., App. Div.).

[227] *Supra*, note 177, s. 3(2)(*b*).

. . . is indebted to the defendant". On the other hand, the Act requires the deponent to swear "*positively* to the indebtedness of the defendant . . . to the plaintiff".[228] It may be argued, therefore, that all the statements that are required to appear in the deponent's affidavit, other than those concerned with the indebtedness of the defendant to the plaintiff, may be statements based on information and belief.

Other legislation simply provides that the affidavit must be made by the plaintiff, his solicitor, or "some other person aware of the facts".[229] While it is not entirely free from doubt that in this case the supporting affidavit may be based entirely on information and belief, it is clear that a deponent relying on information and belief must state the source of his information and the grounds for his belief and, in the context of prejudgment garnishment, the courts have adhered strictly to this requirement.[230]

One problem that has arisen in the context of prejudgment garnishment, but not in the case of attachment, is what to do with money that has been paid into court by a garnishee after a prejudgment garnishment is set aside by the court. The cases on point would seem to be divided, although it should be pointed out that the question has received scant judicial attention. In *Smith v. Metzer*,[231] *Alta. Tractor Parts Ltd. v. Czech Constr. Ltd.*,[232] and *Avco Finance Ltd. v. Suppa*,[233] the money paid into court by the garnishee was ordered to be paid out to the debtor. In *Joncas v. Plotkins*,[234] the Court refused to order payment out to the debtor of the moneys in court, while the Court in *Thomee v. Westcott*[235] decided that money paid into court pursuant to a garnishee summons ought not to be paid out to the debtor in the circumstances under consideration without first giving notice to the garnishee. Finally, in *Boake Realty Ltd. v. Macklin*,[236] the Court ordered the money in court to be returned to the garnishee, commenting that "it is the duty of the court to restore all parties to the same position as they were before the invalid garnishee summons was acted upon".[237]

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[228] *Ibid.*, s. 3(2)(*a*) (emphasis added).

[229] See the *Court Order Enforcement Act*, R.S.B.C. 1979, c. 75, s. 4(1), and the Prince Edward Island Rules, r. 49.14(a). It has been suggested in respect of such a provision that, where the deponent is anyone other than the plaintiff, his affidavit should state that he is "aware of the facts": see *Jaybell Logging Ltd. v. Barzell Logging Co. Ltd.* (1956), 21 W.W.R. 94 (B.C.S.C.).

[230] See, for example, *Adams v. Adams* (1922), 62 D.L.R. 721, [1922] 1 W.W.R. 47 (Alta. S.C., App. Div.) (to ensure that indebtedness by a proposed garnishee is not sworn to upon a mere guess); *Tillicum Athletic Club v. Burick*, [1925] 3 W.W.R. 368 (B.C. Co. Ct.); *McNabb v. Coward*, [1921] 3 W.W.R. 359 (Alta. S.C., T.D.); and *Mel Dunsmore Const'n Ltd. v. Beverage and Foundation Co.* (1960), 31 W.W.R. 427 (Alta. Dist. Ct.).

[231] *Supra*, note 221.

[232] *Ibid.*

[233] (1967), 62 W.W.R. 124 (N.W.T. Terr. Ct.).

[234] *Supra*, note 183.

[235] *Supra*, note 220.

[236] (1968), 67 W.W.R. 113 (Alta. Dist. Ct.).

[237] *Ibid.*, at 116.

3. INJUNCTIVE RELIEF AND RELATED MATTERS

"It is, we think, clear that at the present time an injunction . . . would not be granted to restrain a debtor from disposing of assets or removing them from the jurisdiction."[238] Only six years after this unequivocal statement of the law in England appeared in the *Report of the Committee on the Enforcement of Judgment Debts*,[239] this aspect of the law of creditor and debtor relations was dramatically reversed by a trilogy of cases decided by the English Court of Appeal.[240] In this section, we shall examine the extent to which injunctive relief is now available in England and other Commonwealth jurisdictions to prevent a debtor from disposing of his assets prior to judgment to the detriment of his creditors. The availability of such injunctive relief in Ontario also will be discussed.

(a) THE MAREVA INJUNCTION: RECENT ENGLISH AND COMMONWEALTH DEVELOPMENTS

The right of a creditor to obtain an injunction restraining his debtor from disposing of his assets prior to judgment first was enunciated in the case of *Nippon Yusen Kaisha v. Karageorgis*.[241] The plaintiff in that case, a large Japanese shipowner, sought an interim injunction against the defendants, who had chartered some of the plaintiff's ships, to restrain them from disposing of or removing any of their assets in England. The only asset in England belonging to the defendants, of which the plaintiff was aware, was a fund on deposit with a London bank.

After noting the established practice of the English courts never "to seize assets of a defendant in advance of judgment, or to restrain the disposal of them",[242] Lord Denning M.R. commented as follows:[243]

> It seems to me that the time has come when we should revise our practice. There is no reason why the High Court or this court should not make an order such as is asked for here. It is warranted by s. 45 of the Supreme Court of Judicature (Consolidation) Act 1925[244] which says the High Court may grant a mandamus or injunction or appoint a receiver by an interlocutory order in all cases in which it appears to the court to be just or convenient so to do. It seems to me that this is just such a case. There is a strong prima facie case that the hire is owing and unpaid. If an injunction is not granted, these moneys may be removed out of the jurisdiction and the shipowners will have

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[238] *Report of the Committee on the Enforcement of Judgment Debts* (Cmnd. 3909, 1969), at 324 (hereinafter referred to as the "Payne Committee Report").

[239] *Ibid.*

[240] *Nippon Yusen Kaisha v. Karageorgis*, [1975] 1 W.L.R. 1093, [1975] 3 All E.R. 282 (C.A.); *Mareva Compania Naviera SA v. Int'l Bulkcarriers SA (The Mareva)*, [1975] 2 Lloyd's Rep. 509, [1980] 1 All E.R. 213 (C.A.); and *Rasu Maritima SA v. Perushaan Pertambangan Minyak Dan Gas Bumi Negara (Pertamini)*, [1978] Q.B. 644, [1977] 3 W.L.R. 518, [1977] 3 All E.R. 324 (C.A.).

[241] *Nippon Yusen Kaisha v. Karageorgis*, [1975] 1 W.L.R. 1093, [1975] 3 All E.R. 282 (C.A.) (subsequent references are to [1975] 3 All E.R.).

[242] *Ibid.*, at 283.

[243] *Ibid.*

[244] 15 & 16 Geo. 5, c. 49.

> the greatest difficulty in recovering anything. Two days ago we granted an injunction ex parte and we should continue it.

In *Mareva Compania SA v. International Bulkcarriers SA (The Mareva)*,[245] a case decided one month after *Nippon* and similar on its facts, the English Court of Appeal again acceded to a request for prejudgment injunctive relief. While the defendant challenged the power to grant such relief on the basis of long standing authority,[246] the Master of the Rolls, Lord Denning, focused instead on the language of section 45 of the *Supreme Court of Judicature (Consolidation) Act, 1925*,[247] the provision that is the equivalent of section 19(1) of Ontario's *Judicature Act*.[248] His Lordship was of the opinion that "a creditor who has a right to be paid the debt owing to him, even before he has established his right by getting judgment for it" was possessed of a "legal or equitable right" deserving of protection.[249] Turning to the facts of the case before him, Lord Denning M.R. stated as follows:[250]

> There is money in a bank in London which stands in the name of these charterers. The charterers have control of it. They may at any time dispose of it or remove it out of this country. If they do so, the shipowners may never get their charter hire. The ship is now on the high seas. It has passed Cape Town on its way to India. It will complete the voyage and the cargo will be discharged. And the shipowners may not get their charter hire at all. In face of this danger, I think this court ought to grant an injunction to restrain the charterers from disposing of these moneys now in the bank in London until the trial or judgment in this action. If the charterers have any grievance about it when they hear of it, they can apply to discharge it. But meanwhile the shipowners should be protected. It is only just and right that this court should grant an injunction. I would therefore continue the injunction.

In the last of the trilogy of cases that gave birth to what has come to be known as the "*Mareva* injunction", *Rasu Maritima SA v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara (Pertamina)*,[251] the English Court of Appeal set about establishing the general parameters of this prejudgment remedy. As in the two earlier cases, the plaintiff's claim in *Rasu Maritima* arose out of a charterparty between the plaintiff and the defendant. In response to the plaintiff's claim for damages in the amount of U.S.$3 million for breach of the charterparty, the defendant alleged that the individual who had negotiated the charterparty had acted beyond his authority and had acted in breach of trust.

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[245] *Mareva Compania SA v. International Bulkcarriers SA (The Mareva)*, [1975] 2 Lloyd's Rep. 509, [1980] 1 All E.R. 213 (C.A.) (subsequent references are to [1980] 1 All E.R.).

[246] *Lister & Co. v. Stubbs* (1890), 45 Ch. D. 1 (C.A.).

[247] *Supra*, note 244.

[248] R.S.O. 1980, c. 223, which reads in part as follows:

> 19.-(1) A mandamus or an injunction may be granted or a receiver appointed by an interlocutory order of the court in all cases in which it appears to the court to be just or convenient . . . .

[249] *Supra*, note 245, at 215.

[250] *Ibid.*

[251] *Rasu Maritima SA v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara (Pertamina)*, [1978] Q.B. 644, [1977] 3 W.L.R. 518, [1977] 3 All E.R. 324 (C.A.) (subsequent references are to [1977] 3 All E.R.).

At the time of the plaintiff's action, certain equipment ordered by the defendant sat on the docks at Liverpool. The equipment was valued at U.S.$12 million, but if sold for scrap would fetch only U.S.$350,000. There was some doubt about the ownership of this equipment, that is, whether ownership had passed to the defendant or not. Finally, there was evidence of steps taken by the defendant to dispose of its assets to the Indonesian government.

Although Lord Denning M.R. thought that, on the facts of the case, the relief claimed by the plaintiff was not justified,[252] nevertheless, his support for *Mareva* injunctions was unabated. In his reasons for judgment, His Lordship pointed to the use of foreign attachment in England up until and into the nineteenth century, the widespread reliance on prejudgment attachment in the United States, and the use of a similar procedure in continental Europe. In concluding that the principle that should be applied "to cases where a defendant is out of the jurisdiction but has assets in [England]"[253] should be that applied "by the customary courts in older times and by the courts of the continent today",[254] the Master of the Rolls endorsed the following remarks of Kerr J. in the Court below:[255]

> 'A plaintiff has what appears to be an indisputable claim against a defendant resident outside the jurisdiction, but with assets within the jurisdiction which he could easily remove, and which the court is satisfied are liable to be removed unless an injunction is granted. The plaintiff is then in the following difficulty. First, he needs leave to serve the defendant outside the jurisdiction, and the defendant is then given time to enter an appearance from the date when he is served, all of which usually takes several weeks or even months. Secondly, it is only then that the plaintiff can apply for summary judgment under RSC Ord. 14 with a view to levying execution on the defendant's assets here. Thirdly, however, on being apprised of the proceedings, the defendant is liable to remove his assets, thereby precluding the plaintiff in advance from enjoying the fruits of a judgment which appears irresistible on the evidence before the court. The defendant can then largely ignore the plaintiff's claim in the courts of this country and snap his fingers at any judgment which may be given against him. It has always been my understanding that the purpose and scope of the exercise of this jurisdiction is to deal with cases of this nature. To exercise it on an ex parte basis in such cases presents little danger or inconvenience to the defendant. He is at liberty to apply to have the injunction discharged at any time on short notice.'

Lord Denning M.R. then proposed the following rules regarding *Mareva* injunctions. First, he was of the view that the prejudgment injunctive relief offered by a *Mareva* injunction should not be restricted to cases in which summary judgment was available.[256] Rather, this remedy should be available "whenever the plaintiff can show that he has a 'good arguable case' ".[257] Secondly, he thought that the procedure should apply to restrain the disposition of goods as well as money, although "[c]are should be taken before an injunction is granted over assets which will bring the defendant's trade or business to a standstill or will inflict on him great loss, for that may not be fully compensated for by the undertaking in damages".[258] Finally, Lord Denning M.R. sanctioned the use of a *Mareva* injunction to "encourage" the debtor to put up security for the creditor's claim.[259]

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[252] In this case, the Court concluded that there was substantial uncertainty about the plaintiff's prospects for ultimate success in the action; there was some uncertainty regarding title to the goods in question; and the value of the goods, if seized and sold as scrap, would be minor compared to the enormity of the plaintiff's claim.

[253] *Supra*, note 251, at 333.

[254] *Ibid.*

[255] *Ibid.*, at 333-34.

Insofar as the requirements that must be met before a *Mareva* injunction will issue are concerned, despite some early doubts it is now clear that the remedy is available against a debtor within the jurisdiction as well as a foreign debtor.[260] The nature of the plaintiff's claim – that is, whether it is for a debt or damages – is not relevant: although most of the English cases in which a *Mareva* injunction has been granted may be characterized as commercial cases, tort claims have also given rise to such relief.[261]

The English courts have outlined a host of conditions that must be fulfilled before a claimant will be entitled to a *Mareva* injunction. In *Third Chandris Shipping Corp. v. Unimarine SA*,[262] Lord Denning M.R. set out the following guidelines:[263]

> (i) The plaintiff should make full and frank disclosure of all matters in his knowledge which are material for the judge to know . . . . (ii) The plaintiff should give particulars of his claim against the defendant, stating the ground of his claim and the amount thereof, and fairly stating the points made against it by the defendant. (iii) The plaintiff should give some grounds for believing that the defendants have assets here . . . . (iv) The plaintiff should give some grounds for believing that there is a risk of the assets being removed before the judgment or award is satisfied. The mere fact that the defendant is abroad is not by itself sufficient . . . .[264] Other grounds may be shown for believing

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[256] The Ontario equivalent of summary judgment under Ord. 14 of the English Rules of the Supreme Court 1965 is the procedure for summary judgment under r. 33 of the Supreme Court of Ontario Rules of Practice, *supra*, note 15. It should be noted that the Rules of Civil Procedure proposed by the Civil Procedure Revision Committee contain a much broader summary judgment rule than r. 33: see Williston Committee Rules, *supra*, note 26, r. 22.

[257] *Supra*, note 251, at 334.

[258] *Ibid.*, at 334-35.

[259] *Ibid.*, at 335. See, also, *Allen v. Jambo Holdings Ltd.*, [1980] 1 W.L.R. 1252, [1980] 2 All E.R. 502 (C.A.).

[260] See *Chartered Bank v. Daklouche*, [1980] 1 W.L.R. 107, [1980] 1 All E.R. 205 (C.A.), and *Rahman (Prince Abdul) Bin Turki al Sudairy v. Abu-Taha*, [1980] 1 W.L.R. 1268, [1980] 3 All E.R. 409 (C.A.).

[261] See, for example, *Allen v. Jambo Holdings Ltd.*, *supra*, note 259.

[262] *Third Chandris Shipping Corp. v. Unimarine SA*, [1979] Q.B. 645, [1979] 3 W.L.R. 122, [1979] 2 All E.R. 972 (C.A.) (subsequent references are to [1979] 2 All E.R.).

[263] *Ibid.*, at 984-85.

[264] Insofar as foreign corporations are concerned, Lord Denning M.R. commented as follows (*ibid.*):

> No one would wish any reputable foreign company to be plagued with a Mareva injunction simply because it has agreed to London arbitration. But there

> there is a risk. But some such should be shown. (v) The plaintiffs must, of course, give an undertaking in damages, in case they fail in their claim or the injunction turns out to be unjustified. In a suitable case this should be supported by a bond or security: and the injunction only granted on it being given, or undertaken to be given.

Megarry V.C., in *Barclay-Johnson v. Yuill*,[265] added the following prerequisites to securing a *Mareva* injunction:[266]

> One is that it must appear that there is a danger of default if the assets are removed from the jurisdiction. Even if the risk of removal is great, no Mareva injunction should be granted unless there is also a danger of default. . . .
>
> Second, the plaintiff must establish his claim with sufficient particularity, and show a good arguable case, though he need not demonstrate that his case is strong enough to entitle him to judgment under RSC Ord 14 . . . . Third, the case must be one in which, on weighing the considerations for and against the grant of an injunction, the balance of convenience is in favour of granting it.

More recently, in *Z. Ltd. v. A-Z and AA-LL*,[267] Lord Denning M.R. sought to provide safeguards for third persons who might be affected by the granting of a *Mareva* injunction. These safeguards may be summarized as follows:[268]

> An order served on banks should only apply to accounts held to the extent specified therein, and should not be applicable to joint accounts unless clearly intended to apply to them, this being only justifiable in rare cases . . . .
>
> An order to be served on innocent third parties (and *semble* this would include, as in the instant case, clearing banks which might need to make elaborate searches) should provide expressly to what extent assets in the hands of such parties were affected by the terms of the restraint . . .; the third parties should be told as precisely as possible what they had to do or not to do . . . . The plaintiff should undertake to pay the costs of any searches, and all parties affected should be given the earliest possible opportunity of being heard . . . .

> are some foreign companies whose structure invites comment. We often see in this court a corporation which is registered in a country where the company law is so loose that nothing is known about it, where it does no work and has no officers and no assets. Nothing can be found out about the membership, or its control, or its assets, or the charges on them. Judgment cannot be enforced against it. There is no reciprocal enforcement of judgments. It is nothing more than a name grasped from the air, as elusive as the Cheshire cat. In such cases the very fact of incorporation there gives some ground for believing there is a risk that, if judgment or an award is obtained, it may go unsatisfied. Such registration of such companies may carry many advantages to the individuals who control them, but they may suffer the disadvantage of having a Mareva injunction granted against them. The giving of security for a debt is a small price to pay for the convenience of such a registration. Security would certainly be required in New York. So also it may be in London.

[265] [1980] 1 W.L.R. 1259, [1980] 3 All E.R. 190 (Ch.) (subsequent references are to [1980] 3 All E.R.).

[266] *Ibid.*, at 195.

[267] [1982] 2 W.L.R. 288, [1982] 1 All E.R. 556 (C.A.).

[268] See Starke, "The Scope of the 'Mareva' Injunction Defined and Enlarged" (1982), 56 Aust. L.J. 199, at 200.

These conditions would be in addition to any undertaking by the applicant with respect to damages that might be suffered by a stranger to the action or the expense to which a third person subject to the injunction might be put.[269]

In addition to the conditions for a *Mareva* injunction, the English courts have considered a number of related issues. Perhaps the most important of these is the nature of the relief provided by a *Mareva* injunction. It is now clear that a *Mareva* injunction does not give the enjoining creditor any interest in the debtor's property: "[i]t merely restrains the owner from dealing with the asset in certain ways".[270] In coming to this conclusion, Buckley L.J., in *Cretanor Maritime Co. Ltd. v. Irish Marine Mngt. Ltd.*,[271] compared prejudgment injunctive relief and attachment. The latter, he said, meant "a seizure of assets under some writ or like command or order of a competent authority, normally with a view to their being realized to meet an established claim or held as a pledge or security for the discharge of some claim, either already established or yet to be established".[272] A *Mareva* injunction, on the other hand, "even if it relates only to a particularised asset . . . is relief in personam. It does not effect a seizure of any asset."[273] Accordingly, in the *Cretanor* case, which involved a dispute between a creditor having the benefit of a *Mareva* injunction and a prior debenture holder, Buckley L.J. decided that the rights of the creditor in the enjoined fund had to give way to prior rights therein, and that the injunction should be discharged.

The limited purpose of prejudgment injunctive relief can also be seen from the case of *Iraqi Ministry of Defence v. Arcepey Shipping Co. SA*.[274] Some time after the plaintiff had obtained a *Mareva* injunction in respect of the proceeds of certain insurance policies in favour of the defendant, another of the defendant's creditors sought to have the terms of the injunction varied to allow its claim to be satisfied from these proceeds. This other creditor had not secured a judgment against the defendant, and its claim was unsecured.

Robert Goff J. granted the intervenor's request on the following basis. In his view, "the fundamental purpose of the *Mareva* jurisdiction is to prevent foreign parties from causing assets to be removed from the jurisdiction in order to avoid the risk of having to satisfy any judgment which may be entered against them in pending proceedings in this country".[275] This jurisdiction was not exercised "to improve the position of claimants in an insolvency".[276] Consequently, Robert Goff J. saw nothing wrong with varying a *Mareva* injunction "to allow a transfer of assets by the defendant if the defendant satisfies the court that he requires the money for a purpose which does not conflict with the policy underlying the *Mareva* jurisdiction".[277] Indeed, he thought that it did not make "commercial sense that a party claiming unliquidated damages should . . . prevent the defendant from using his assets to satisfy his debts as they fall due and be put in the position of having to allow his creditors to proceed to judgment with consequent loss of credit and of commercial standing".[278]

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[269] See, for example, *Searose Ltd. v. Seatrain U.K. Ltd.*, [1981] 1 W.L.R. 894, [1981] 1 All E.R. 806 (Q.B.), and *Clipper Maritime Co. Ltd. of Monrovia v. Mineralimportexport*, [1981] 1 W.L.R. 1262, [1981] 3 All E.R. 664 (C.A.). See, also, the recent case, *Project Development Co. Ltd. S.A. v. K.M.K. Securities Ltd.*, [1982] 1 W.L.R. 1470 (Q.B.), where Parker J. considered the extent to which a third party should be indemnified for legal costs incurred as a result of the granting of a *Mareva* injunction.

[270] *Cretanor Maritime Co. Ltd. v. Irish Marine Mngt. Ltd.*, [1978] 1 W.L.R. 966, [1978] 3 All E.R. 164 (C.A.), at 170, *per* Buckley L.J. (subsequent references are to [1978] 3 All E.R.).

[271] *Ibid.*

[272] *Ibid.*, at 170.

[273] *Ibid.*

[274] *Iraqi Ministry of Defence v. Arcepey Shipping Co. SA*, [1980] 2 W.L.R. 488, [1980] 1 All E.R. 480 (Q.B.) (subsequent references are to [1980] 1 All E.R.). See, also, *A. v. C. (No. 2)*, [1981] 2 W.L.R. 634, [1981] 2 All E.R. 126 (Q.B.).

The English courts have also recognized the importance of providing an applicant for a *Mareva* injunction, in appropriate circumstances, with the right to discover the defendant as to his means and assets.[279] While there is a division of opinion concerning the circumstances in which this unique right of discovery should be available, there is a recognition of the utility of such a right in making a *Mareva* injunction fully effective, and in reducing the costs of compliance by third persons or strangers to the action.

Although welcomed by the English courts, the *Mareva* injunction has not met with universal approval in other parts of the Commonwealth. For example, although the *Mareva* injunction jurisdiction has been adopted in most Australian states, its reception in some cases has been less than enthusiastic. Until recently, the New South Wales courts, in particular, embraced the authority to restrain a debtor from dealing with assets prior to judgment only begrudgingly and not on its merits, but rather on the ground that they were bound by the decisions of the English Court of Appeal.[280]

The Supreme Court of the State of South Australia, in *Pivovaroff v. Chernabaeff*,[281] refused to grant a *Mareva* injunction on the ground that this remedy was not available in the case of a resident, as opposed to a foreign, defendant. As we have seen,[282] the English courts, in recent years, have rejected such a distinction, and a *Mareva* injunction will be granted in an appropriate case as readily where the defendant is a resident as where he is outside the jurisdiction. It should be pointed out that Bray C.J., in *Pivovaroff v. Chernabaeff*, also expressed serious reservations regarding *Mareva* injunctions. In his opinion, the introduction of the jurisdiction to grant such relief was a matter for the legislature and not for the courts. In this connection, he noted the existence in South Australia of absconding debtors legislation as an indication that courts were preempted from creating such a prejudgment remedy.

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[275] *Ibid.*, at 485.

[276] *Ibid.*, at 486.

[277] *Ibid.*

[278] *Ibid.*

[279] See *A. v. C.*, [1981] 2 W.L.R. 629, [1980] 2 All E.R. 347 (Q.B.); *A.J. Bekhor & Co. Ltd. v. Bilton*, [1981] 2 W.L.R. 601, [1981] 2 All E.R. 565 (C.A.); and *Z. Ltd. v. A-Z and AA-LL*, *supra*, note 267. The need for a right of discovery is less urgent in Ontario because of the existence of r. 230 of the Rules of Practice, *supra*, note 15, which provides that "[a]ny party may by subpoena require the attendance of a witness to be examined . . . for the purpose of using his evidence upon any motion".

[280] See *Ex parte B.P. Exploration Co. (Libya) Ltd., Re Hunt*, [1979] 2 N.S.W.L.R. 406 (S.C.); *Balfour Williamson (Australian) Pty. Ltd. v. Douterluigne*, [1979] 2 N.S.W.L.R. 884 (S.C.); and *Turner v. Sylvester*, [1981] 2 N.S.W.L.R. 295 (S.C.). See, however, the recent decision of the New South Wales Court of Appeal in *Riley McKay Ltd. v. McKay*, [1982] 1 N.S.W.L.R. 264.

[281] (1978), 16 S.A.S.R. 329 (S.C.).

[282] See *supra*, this sec.

In contrast to the view of Bray C.J. in *Pivovaroff* are the cases of *Sanko Steamship Co. and D.C. Commodities (A'asia) Pty. Ltd.*[283] and *Praynovsky v. Sablyack*,[284] in which the Western Australia Supreme Court and Victoria Supreme Court, respectively, affirmed the existence of the authority to grant a *Mareva* injunction. The New Zealand Supreme Court, in *Hunt v. B.P. Exploration Co. (Libya) Ltd.*,[285] also recognized that, given modern conditions, there was a need for the *Mareva* injunction jurisdiction. Barton J. commented as follows:[286]

> The Court has to approach modern problems with the flexibility of modern business. In former times, as Lawton L.J. pointed out, it would have been more difficult for a foreign debtor to take his assets out of the country. Today, vast sums of money can be transferred from one country to another in a matter of seconds as a result of a phone call or a telex message. Reputable foreign debtors of course have nothing to fear: the facts of the reported *Mareva* cases indicate that the jurisdiction is wholesome; the sheer number of *Mareva* injunctions granted in London indicates that the jurisdiction is fulfilling a need.

(b) THE MAREVA INJUNCTION: RECENT CANADIAN DEVELOPMENTS

Until very recently, courts in Canada took little notice of the developments in the law of prejudgment remedies in England. Indeed, before 1980, the *Mareva* injunction line of cases had been considered in only one Ontario case, *OSF Industries Ltd. v. Marc-Jay Investments Inc.*[287] In that case, Lerner J. dismissed the plaintiff's application under section 19(1) of the *Judicature Act*[288] for an injunction to restrain the defendant from removing its assets from the jurisdiction. Mr. Justice Lerner believed himself bound by an earlier Ontario Court of Appeal decision, *Bedell v. Gefaell (No. 2)*.[289] In that case the Ontario Court of Appeal, in accordance with earlier authorities, had refused to grant a *Mareva*-like injunction, despite the broad language of the precursor to section 19(1) of the *Judicature Act* – that an injunction may be granted ". . . in all cases in which it appears to the court to be just or convenient". Lerner J., however, recognized the utility of such prejudgment injunctive relief, commenting that he did

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[283] [1980] W.A.R. 51 (S.C.).

[284] [1977] V.R. 114 (S.C.).

[285] [1980] 1 N.Z.L.R. 104 (S.C.).

[286] *Ibid.*, at 118.

[287] *OSF Industries Ltd. v. Marc-Jay Investments Inc.* (1978), 20 O.R. (2d) 566 (H.C.J.).

[288] R.S.O. 1970, c. 228. See, now, R.S.O. 1980, c. 223.

[289] [1938] O.R. 726, [1938] 4 D.L.R. 443 (C.A.).

"sympathize with the fact that a judgment when gained may ultimately be defeated by a defendant's conduct *pendente lite*".[290]

Since its initial setback in the *OSF Industries Ltd.* case, the *Mareva* injunction jurisdiction has generally come to be accepted by Ontario and other Canadian courts. However, Ontario courts in particular have been quick to point out that they have always had the authority to grant an injunction to restrain a defendant from disposing of his assets in two kinds of case, that is, where the injunction is sought to preclude the defendant from making a fraudulent conveyance,[291] and where the plaintiff's claim is based on an allegation of fraud.[292]

The first Ontario case to approve of the *Mareva* injunction jurisdiction was *Liberty National Bank & Trust Co. v. Atkin*.[293] There was no allegation of fraud in that case; nor was the injunction sought to preclude a fraudulent conveyance. Rather, there was a concern on the part of the plaintiff that, if a *Mareva* injunction were not granted, the defendants would simply remove from the jurisdiction the moneys held by them in the form of a term deposit. After a review of the relevant English and Canadian authorities, Montgomery J. decided to follow the *Mareva* line of authorities because, in his opinion, "the winds of change cry out for the new equitable remedy that *Mareva* provides".[294] He was of the view that a *Mareva* injunction should be available "if there is a danger of the defendant absconding or of the assets being removed out of the jurisdiction or disposed of within the jurisdiction, or otherwise dealt with so that if the plaintiff obtains judgment he may not be able to have it satisfied".[295]

Prior to and since the decision of Montgomery J. in the *Liberty National Bank* case, there have been a number of decisions in which the *Mareva* injunction jurisdiction has been examined. Some were cases where similar injunctive relief was available under one of the more traditional bases for restraining a defendant from dealing with his assets to the detriment of the plaintiff.[296] In others, the court has refused to issue a *Mareva* injunction because one or more of the conditions therefor were not satisfied.[297] In a small number of cases, the court was convinced that the issuance of a *Mareva* injunction was warranted.[298]

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[290] *Supra*, note 287, at 568.

[291] See, for example, *Robert Reiser & Co. Inc. v. Nadore Food Processing Equipment Ltd.* (1977), 17 O.R. (2d) 717, 81 D.L.R. (3d) 278 (H.C.J.).

[292] See, for example, *Mills v. Petrovic* (1980), 30 O.R. (2d) 238, 118 D.L.R. (3d) 367 (H.C.J.), and *Canadian Pacific Airlines Ltd. v. Hind* (1981), 32 O.R. (2d) 591, 122 D.L.R. (3d) 498 (H.C.J.).

[293] (1981), 31 O.R. (2d) 715, 121 D.L.R. (3d) 160 (H.C.J.) (subsequent references are to 31 O.R. (2d)).

[294] *Ibid.*, at 723.

[295] *Ibid.* See, also, *Rahman (Prince Abdul) Bin Turki al Sudairy v. Abu-Taha*, *supra*, note 260.

[296] See, for example, *Canpotex Ltd. v. Graham*, unreported (February 5, 1982, Ont. H.C.J.).

[297] See, for example, *Erie Mfg. Co. (Canada) Ltd. v. Rogers* (1981), 24 C.P.C. 132 (Ont. H.C.J.).

[298] *Quinn v. Marsta Cession Services Ltd.* (1981), 34 O.R. (2d) 659, 16 B.L.R. 126 (H.C.J.), leave to appeal granted (1982), 16 B.L.R. 131 (Ont. H.C.J.), and *Van Brugge v. A. Frommer International Ltd.* (1982), 35 O.R. (2d) 333 (H.C.J.), leave to appeal granted.

Undoubtedly, the most important case since *Liberty National Bank* was decided is *Chitel v. Rothbart*,[299] a decision of the Ontario Court of Appeal. While the comments of MacKinnon A.J.C.O., delivering the judgment of the Court, are *obiter dicta*,[300] they are nonetheless quite significant, as they acknowledge that "[t]he Mareva injunction . . . is here to stay and properly so".[301] MacKinnon A.C.J.O. cautioned against indiscriminate resort to the *Mareva* injunction remedy. He suggested, for example, that a plaintiff applying for a *Mareva* injunction must persuade the court that he has "a strong *prima facie* case on the merits".[302] And his description of the circumstances in which such relief is available would seem to be slightly more limited than the test enunciated by Montgomery J. in the *Liberty National Bank* case. MacKinnon A.C.J.O. stated:[303]

> The applicant must persuade the court by his material that the defendant is removing or there is a real risk that he is about to remove his assets from the jurisdiction to avoid the possibility of a judgment, or that the defendant is otherwise dissipating or disposing of his assets, in a manner clearly distinct from his usual or ordinary course of business or living, so as to render the possibility of future tracing of the assets remote, if not impossible in fact or in law.

Insofar as the rest of Canada is concerned, the *Mareva* injunction jurisdiction has been considered, expressly or implicitly, in British Columbia, Manitoba, New Brunswick, the Northwest Territories, and Nova Scotia.[304] The Federal Court of Canada also has had occasion to examine the appropriateness of such prejudgment injunctive relief.[305] Only in Manitoba has the court commented unfavourably on the concept of a prejudgment injunction to prevent a defendant from disposing of or dealing with his assets prior to judgment.

(c) RESTRAINING ORDERS UNDER THE *FAMILY LAW REFORM ACT*

A power akin to that exercised by the courts under their *Mareva* jurisdiction can be found in Ontario in the *Family Law Reform Act*.[306] Section 9 of the Act empowers a court, in or pending an application for the division of family or non-family assets, for the determination of any question as to ownership or right to possession of any particular property, or for the determination of the contribution of a spouse or former spouse to the acquisition, management, maintenance, operation, or improvement of property other than family assets, to make "such interim order as it considers necessary for restraining the dissipation of the property [in question] and for the possession, delivering up, safekeeping and preservation of the property". In or pending an application for support, the court is authorized by section 22 of the Act to make "such interim or final order as it considers necessary for restraining the disposition or wasting of assets that would impair or defeat the claim or order for the payment of support". While the former power would be used to secure property that is the subject matter of an action,[307] the latter is much more akin to the *Mareva* jurisdiction: a support application involves no claim to specific property.

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[299] *Chitel v. Rothbart*, unreported (December 2, 1982, Ont. C.A.). The case was referred to the Court of Appeal by Anderson J. pursuant to section 34 of the *Judicature Act*, *supra*, note 27: see *Chitel v. Rothbart* (1982), 36 O.R. (2d) 124 (H.C.J.).

[300] The plaintiff's application was dismissed on the grounds that she had failed to make full and frank disclosure on the original *ex parte* application for a *Mareva* injunction.

[301] *Chitel v. Rothbart*, unreported (December 2, 1982, Ont. C.A.), at 44. It should be noted that the Court of Appeal was of the view that Lerner J. had erred in *OSF Industries Ltd. v. Marc-Jay Investments Inc.*, *supra*, note 287, in holding there was no basis in law for *Mareva* injunctions.

[302] *Chitel v. Rothbart*, unreported (December 2, 1982, Ont. C.A.), at 42.

[303] *Ibid.*, at 41-42.

[304] B.C.: *Manousakis v. Manousakis* (1979), 10 B.C.L.R. P-21 (S.C.), and *Dean v. Ford Credit Ltd.* (1982), 43 C.B.R. (N.S.) 14 (B.C.S.C.); Man.: *Hawes v. Szewczyk*, unreported (April 18, 1979, Man. Q.B.); N.B.: *Humphreys v. Buraglia* (1982), 135 D.L.R. (3d) 535, 39 N.B.R. (2d) 674 (C.A.). See, also, *Irving Oil Ltd. v. Biornstad, Biorn, & Co.* (1981), 35 N.B.R. (2d) 265 (Q.B., T.D.); N.W.T.: *B.P. Exploration Co. (Libya) Ltd. v. Hunt* (1980), 114 D.L.R. (3d) 35, [1981] 4 W.W.R. 209 (N.W.T.S.C.); and N.S.: *Parmar Fisheries Ltd. v. Parceria Maritima Esperenca L. DA.*, unreported (October 4, 1982, N.S.S.C.).

[305] *Elesguro Inc. v. Ssangyong Shipping Co. Ltd.*, [1981] 2 F.C. 326, (1980), 117 D.L.R. (3d) 105 (T.D.).

There have been very few reported cases in which a court has had to consider the scope of either or both of these sections. Undoubtedly, the most important decision to date concerning the operation of section 9 is *Mageau v. Mageau*.[308] Walsh J. in that case rejected the view that "there must be an essential ingredient of urgency"[309] before a section 9 order will be granted in respect of family assets. Given the policy underlying the *Family Law Reform Act*, Walsh J. concluded that, in the case of family assets, orders under section 9 "should be made as a matter of course".[310] Insofar as non-family assets are concerned, Mr. Justice Walsh adopted a different position. Since "there is no underlying premise in the legislation that [such] assets are to be equally shared",[311] Walsh J. held that there must be "an essential ingredient of urgency", and indicated that "there will be a considerable onus on the applicant to establish that circumstances exist which call for the granting of an interim order under s. 9".[312]

(d) DEFAULT JUDGMENTS AND EXECUTION

Where an action has been commenced by specially endorsed writ pursuant to Rule 33 of the Ontario Rules of Practice,[313] the plaintiff may sign judgment against the defendant if he fails to file an appearance[314] or a statement of defence.[315] However, Rule 526 provides that "[a]ny judgment by default may be set aside on motion". Although not all Ontario courts embraced *Mareva* injunctions, the same courts for years sanctioned analogous prejudgment relief when setting aside a judgment obtained by default. This the courts have done by allowing a writ of *fi.fa.* obtained by the successful plaintiff to stand even after his default judgment has been set aside.

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[306] *Supra*, note 43. In its *Report on Family Law*, Part VI, *Support Obligations* (1975), at 132-33, the Ontario Law Reform Commission recommended that "the Supreme Court of Ontario should have the power in maintenance proceedings, either before or after judgment, to enjoin the apprehended disposition of property by a spouse which is intended to defeat a claim for maintenance, or to prevent the enforcement of a maintenance order".

[307] This power is similar to the power to order the preservation of property that is the subject matter of an action: see discussion *supra*, sec. 2(a)(iv).

[308] *Mageau v. Mageau* (1978), 22 O.R. (2d) 179, 8 R.F.L. (2d) 282 (H.C.J.) (subsequent references are to 22 O.R. (2d)). See, also, *Richie v. Richie* (1979), 23 O.R. (2d) 360 (Co. Ct.); *Richards v. Richards* (1978), 1 F.L.R.A.C. 134 (Ont. Prov. Ct. (F.D.)); and *Patti v. Patti* (1982), 37 O.R. (2d) 209 (Master S.C.O.).

[309] *Mageau v. Mageau*, *supra*, note 308, at 181.

[310] *Ibid.*

[311] *Ibid.*, at 182.

[312] *Ibid.*

[313] Rules of Practice, *supra*, note 15.

This practice was challenged recently in *Jet Power Credit Union Ltd. v. McInally*[316] and *Canadian Imperial Bank of Commerce v. Sheahen.*[317] In the former case, O'Driscoll J., while acknowledging that a court setting aside a default judgment may impose onerous terms, including payment into court of the disputed sum, held that the court had no jurisdiction to continue a writ of execution. His reasoning was as follows:[318]

> Execution owes its validity to the existence of an unpaid judgment. Once a judgment, upon which the writ of execution is based is set aside, the execution ceases to be valid and the Court in the exercise of its jurisdiction cannot impose a term that 'the execution stands as security pending trial, but that its operation be stayed' because such an order would be self-contradictory.

Soon after *Jet Power* was decided, Hughes J., in *Canadian Imperial Bank of Commerce v. Sheahen*, reaffirmed the former practice, concluding that *Jet Power* had been wrongly decided. His view was based on the theory that a writ of *fi. fa.* has an existence independent of the judgment upon which it is based:[319]

> If, therefore, it is conceded, as I think it must be, that a writ of *fieri facias* has a separate existence and is not merely an appendage to judgment, there is nothing in my view which inhibits the procedure resorted to by so many Judges and Masters of this Court,[320] and one which must be well within its inherent powers.

Whether Mr. Justice Hughes' view of writs of execution is right or wrong,[321] the Ontario practice that he approved in *Sheahen* is followed in many of the provinces at the present time. As was mentioned by Hughes J.

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[314] *Ibid.*, rr. 42(5) and 51.

[315] *Ibid.*, r. 53.

[316] (1973), 17 O.R. (2d) 59 (H.C.J.).

[317] (1978), 22 O.R. (2d) 686 (Div. Ct.).

[318] *Supra*, note 316, at 64.

[319] *Supra*, note 317, at 691.

[320] See, for example, *Brown v. Coleman Development Co.* (1913), 4 O.W.N. 728, 23 O.W.R. 946 (S.C.); *Hunter v. Perrin* (1917), 12 O.W.N. 200 (H.C. Div.); *Teasdale v. Welsh* (1920), 19 O.W.N. 246 (H.C. Div.); *Pillon v. Meloche* (1922), 21 O.W.N. 415 (H.C. Div.); *Staples and Bell Inc. v. Canadian Coal Supply* (1925), 28 O.W.N. 286 (H.C. Div.); and *Briar Investments Ltd. v. Mintz*, [1971] 2 O.R. 747 (Master S.C.O.). See, also, *Whelihan v. Kehoe* (1910), 2 O.W.N. 166, 17 O.W.R. 202 (H.C. Div.).

[321] For a discussion of this point, see Springman, "*Canadian Imperial Bank of Commerce v. Sheahen*: Setting Aside Default Judgment on Terms that any Writ Stand Pending Disposition of the Action" (1982), 3 Advocates' Q. 365.

in the *Sheahen* case, Alberta courts have adopted this practice.[322] It would appear that, on occasion, the Saskatchewan courts also have ordered default judgments to be set aside upon terms, including a condition that the judgment and execution stand as security for the plaintiff's claim.[323] In Nova Scotia, it would seem that a similar procedure is available. In *Irving Oil Ltd. v. Hearn*,[324] the Appellate Division of the Nova Scotia Supreme Court approved the imposition of an order restraining the disposition of the defendant's real property in Nova Scotia until the final adjudication of the plaintiff's claim. It should be noted, however, that the defendant's counsel did not oppose the imposition of this condition.

It would appear that the policy underlying the *Sheahen* decision is similar, if not identical, to the reasons behind the creation and extension of the *Mareva* injunction in England. In each case, the courts seem to have been motivated by a desire "to ensure that, if the plaintiff succeeds in the action, there will be property of the defendant available [in the jurisdiction] out of which the judgment which the plaintiff obtains in it can be satisfied".[325]

4. PREJUDGMENT ARREST OF THE DEBTOR

Another provisional remedy that the Commission has examined is arrest of the debtor. The authority of a creditor to arrest his debtor before judgment has a long and inglorious past, which need not be discussed here.[326] Suffice it to say that, in Ontario at the present time, prejudgment arrest is confined by statute to a narrow set of circumstances. We now turn to a brief analysis of the relevant legislation, the *Fraudulent Debtors Arrest Act*[327] and the *Family Law Reform Act*.[328]

The key provision of the *Fraudulent Debtors Arrest Act* is section 2(1), which sets out the jurisdictional facts that must be established before a creditor may resort to the remedy of prejudgment arrest. Section 2(1) reads as follows:

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[322] *Cotton v. Dempster*, [1925] 1 W.W.R. 954 (Alta. S.C.).

[323] *Bank of Montreal v. Herrmann*, [1975] 2 W.W.R. 368 (Sask. Q.B.), citing *Sales v. Sereda* (1952), 5 W.W.R. 470 (Sask. Q.B.).

[324] (1978), 31 N.S.R. (2d) 378, 52 A.P.R. 378 (S.C., App. Div.).

[325] *The Rena K*, [1979] Q.B. 377, [1978] 3 W.L.R. 431, [1979] 1 All E.R. 397, at 417, *per* Brandon J.

[326] For a discussion of the arrest of debtors in the early common law, see Sutherland, "Mesne Process upon Personal Actions in the Early Common Law" (1966), 82 L.Q. Rev. 482. See, also, Freedman, "Imprisonment for Debt" (1927-28), 2 Temple L.Q. 330; Ford, "Imprisonment for Debt" (1926-27), 25 Mich. L. Rev. 24; and Note, "Body Attachment and Body Execution: Forgotten but not Gone" (1975-76), 17 Wm. & M.L. Rev. 543. A brief history of this area of the law of enforcement also is contained in the Australian Government Commission of Inquiry into Poverty, *Debt Recovery in Australia* (1977), ch. 3.

[327] *Supra*, note 42. The Act has remained substantially the same since 1911. Similar legislation is to be found in a number of the other provinces: see, for example, *Arrest and Examinations Act*, R.S.N.B. 1973, c. A-12; *The Judicature Act*, R.S.N. 1970, c. 187, ss. 100-08; and the *Bailable Proceedings Act*, R.S.P.E.I. 1974, c. B-1, ss. 5 *et seq.*

[328] *Supra*, note 43, s. 24.

> 2.-(1) When a person by affidavit of himself or some other person shows to the satisfaction of a judge of the Supreme Court or of a county court that he has a cause of action against a person liable to arrest to the amount of not less than $100, and also such facts and circumstances as satisfy the judge that there is a good and probable cause for believing that such person, unless he be forthwith apprehended, is about to quit Ontario with intent to defraud his creditors generally or the applicant in particular, the judge may order that the person against whom the application is made be arrested and give security for such sum as the judge thinks fit.

The jurisdictional facts outlined in this provision are three in number: (1) proof of the existence of a cause of action in an amount not less than $100; (2) proof that the debtor is liable to arrest;[329] and (3) proof that there is a good and probable cause for believing that the debtor, unless apprehended immediately, is about to quit Ontario with intent to defraud his creditors generally or the applicant in particular. Unlike attachment under the *Absconding Debtors Act*, it would appear that arrest is available in respect of all causes of action, not only actions for debt.

It should be noted that arrest of a debtor is available both before and after the commencement of an action.[330] However, in the case of an order for arrest made prior to the initiation of legal proceedings, the order will expire unless an action is commenced within two days thereof, or within such further time as the judge by order allows.[331] An order for arrest remains in force for two months, and a new order may be obtained upon the expiration of any order for arrest.[332] To effect the debtor's arrest, the plaintiff must deliver the order for arrest to the sheriff and direct him to arrest the debtor.[333]

Where a debtor has been arrested before judgment pursuant to the *Fraudulent Debtors Arrest Act*, he may secure his release from custody by delivering to the sheriff a certificate indicating compliance with the security provision of the order for arrest.[334] The Act provides that security may be given by payment into court of the amount mentioned in the order for arrest, or by a bond given to the plaintiff by the defendant and two sufficient sureties.[335] Security may also take any other form agreed to by the plaintiff.[336] Where a bond is used, its conditions should be that the defendant will pay to the plaintiff the amount adjudged to be owing in the action or that he will surrender himself into custody.[337] The bond must also be approved by some judicial official, after notice thereof has been given to the plaintiff or his solicitor.[338]

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[329] See, for example, sections 11 and 13 of the *Fraudulent Debtors Arrest Act*, *supra*, note 42, which make certain persons immune from arrest for the purposes of the Act.

[330] See *Fraudulent Debtors Arrest Act*, *supra*, note 42, s. 2(3).

[331] *Ibid.*, s. 2(4).

[332] *Ibid.*, s. 3.

[333] *Ibid.*, s. 8. The order must be executed within 2 months of its having been made: see s. 9.

[334] *Ibid.*, s. 20(2). Section 2(1), reproduced above, provides that the judge may order the arrest of the debtor and the giving of security by him in the amount specified in the order.

[335] *Ibid.*, s. 14.

[336] *Ibid.*

[337] *Ibid.*, s. 15.

Reference has been made to the fact that an order for arrest may be obtained prior to the commencement of an action by a creditor, and that, in such a case, under section 2(4) of the *Fraudulent Debtors Arrest Act*, legal proceedings must be instituted within two days of the making of the order, or such further time as the judge by order allows. Failure to institute legal proceedings within the time permitted will result in the discharge of the debtor. Once the debtor has been taken into custody, the plaintiff, if he has not done so already, must deliver his statement of claim within one month after the arrest or within the time prescribed by the Ontario Rules of Practice,[339] whichever is the earlier date.[340] Once again, failure to comply with this statutory requirement will result in the defendant being discharged out of custody.[341]

In addition to permitting a debtor to secure his release from custody by complying with the security provisions of the order for arrest,[342] the *Fraudulent Debtors Arrest Act* allows a person arrested to apply for his discharge from custody. Section 24 of the Act provides as follows:

> 24.-(1) A person arrested upon an order for arrest may apply to the court or a judge for an order that he be discharged out of custody, and the court or judge, subject to appeal, may make such order thereon as seems just.
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> (2) A judge of a county court making an order for arrest, whether in the Supreme Court or in his own court, shall, in respect of such order and the arrest made thereupon, possess all the powers of a judge of the Supreme Court under this section, and may in like manner, on application to him, order the defendant to be discharged out of custody, or make such order therein as to him seems just.
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> (3) Any such order made by a judge of the county court may be discharged or varied by the Divisional Court.

The remainder of the Act, some thirty sections,[343] is primarily concerned not with prejudgment arrest of the debtor, but with postjudgment arrest under a writ of *capias ad satisfaciendum*. These provisions are beyond the scope of this chapter and will not be examined here.[344]

Prejudgment arrest under the *Family Law Reform Act* is authorized by section 24 thereof. This section reads as follows:

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[338] *Ibid.*, s. 18. Unless otherwise directed, there must be at least 48 hours notice. The judicial officers referred to in this section are the proper officers in the office in which the action was commenced, the local judge, or the master.

[339] *Supra*, note 15, r. 43.

[340] *Fraudulent Debtors Arrest Act*, *supra*, note 42, s. 21.

[341] *Ibid.*

[342] See *supra*, notes 334-38 and accompanying text.

[343] *Fraudulent Debtors Arrest Act*, *supra*, note 42, ss. 27-58.

[344] For a discussion of postjudgment arrest and imprisonment as an enforcement remedy, see Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

> 24. Where an application is made under section 18 . . . and a judge of the court is satisfied that the respondent . . . is about to leave Ontario, the judge may issue a warrant in the form prescribed by the rules of the court for the arrest of the respondent . . . .

Section 18 of the *Family Law Reform Act* is concerned with support orders.

It has been held that section 24 does not authorize prejudgment arrest of a respondent where the only claim made is for a division of family or non-family assets.[345] It also should be noted that section 24 of the *Family Law Reform Act*, unlike section 2(1) of the *Fraudulent Debtors Arrest Act*, does not require the applicant to show that the respondent is about to leave the jurisdiction with the intent of defrauding the applicant. Finally, unlike the *Fraudulent Debtors Arrest Act*, the *Family Law Reform Act* does not prescribe the rights of an arrested respondent to secure his release.

The above description of prejudgment arrest has been a cursory one for reasons that will become apparent when recommendations for reform of the law of enforcement pertaining to prejudgment remedies are considered.

5. THE CASE FOR REFORM

In the preceding sections, we have described in some detail the different prejudgment remedies that now form part of the law of Ontario. Our consideration of this area of the law of the enforcement of judgment debts has led us to conclude that reform is long overdue, and that the changes must be substantial in nature. Fundamental reform is necessary for at least five discrete reasons.

First, the fact is that most of the provisional relief legislation that we have examined is at least seventy years old and substantially unaltered from the time of its original enactment. The *Absconding Debtors Act* has been in its present form since 1909; the *Fraudulent Debtors Arrest Act* since 1911. The language of these statutes is outdated and in some cases archaic. However, these criticisms alone would hardly justify anything more than cosmetic changes.

A second, more substantive reason for fundamental reform is related to the changes in society and technology since, for example, the *Absconding Debtors Act* first was enacted over 150 years ago. The assumptions upon which this legislation was based are no longer as valid as they once may have been. Travel, both national and international, is infinitely easier today than in the mid-nineteenth century. Instant telecommunications were only dreamed of in the Victorian era.

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[345] See *Cullen v. Cullen* (1980), 30 O.R. (2d) 551, 117 D.L.R. (3d) 746 (H.C.J.). An applicant claiming a division of assets, however, could resort to the *Fraudulent Debtors Arrest Act*, *supra*, note 42.

The English courts, in creating and developing the *Mareva* jurisdiction that now forms an integral part of the law of enforcement in England, have been influenced greatly by the transformations in society and technology that have characterized the second half of the twentieth century. The following words of Lawton L.J., in *Third Chandris Shipping Corp. v. Unimarine SA*,[346] are particularly appropriate:[347]

> Nowadays defaulting on debts has been made easier for the foreign debtor by the use of corporations, many of which hide the identities of those who control them, and of so-called flags of convenience, together with the development of world-wide banking and swift communications. By a few words spoken into a radio telephone or tapped out on a telex machine bank balances can be transferred from one country to another and within seconds can come to rest in a bank which is untraceable or, even if known, such balances cannot be reached by any effective legal process.
>
> . . . .
>
> Once a writ is issued, a debtor who intends to default will do what he can to avoid having to meet his obligations. The British defaulter may try to dissipate his assets; he may succeed to some extent but retribution in the form of either bankruptcy or liquidation will probably come about one day. Until recently the prospects for the defaulting foreigner were much better. A telephone call or telex message could within seconds of the service of a writ, or knowledge that a writ had been issued, put all liquid assets out of the reach of the creditor. It was these considerations which led this court to exercise the jurisdiction given by s. 45 of the Supreme Court of Judicature (Consolidation) Act 1925 to issue ex parte injunctions whenever it was just or convenient to do so, the cause of action itself being triable within the jurisdiction.

We believe, as did the English courts responsible for the *Mareva* injunction, that the advent of such things as supersonic flight and instant, intercontinental telecommunications, among others, require new approaches to the subject of prejudgment relief.

The ineffectiveness of the traditional existing prejudgment remedies available to unsecured creditors is the third reason that has convinced the Commission of the need for reform. Consider the following example. Assume that a debtor is preparing to remove his assets from the jurisdiction with the express intent of defeating his creditors. Under the *Absconding Debtors Act*, the creditors would be remediless in such a case. As we have pointed out earlier, attachment of a debtor's property is possible only after the debtor himself has departed from the jurisdiction. There are probably few debtors who quit the Province with intent to defraud their creditors leaving behind exigible property.

Fourthly, the present law, lacking any coherent philosophical underpinning, has given rise to some unjustifiable inconsistencies. Compare, for example, the refusal of the courts – at least until very recently – to grant prejudgment injunctive relief and the judicial approval of prejudgment execution where a default judgment is set aside. Such incongruity, in our view, cannot be rationalized.

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[346] *Supra*, note 262.

[347] *Ibid.*, at 986.

Finally, the Commission has been impressed by the hardship to creditors and debtors alike that flows from the present state of the law. We already have mentioned some of the problems that creditors may encounter in securing provisional relief. Moreover, procedural safeguards to provide debtors with protection from abuse of existing prejudgment remedies are inadequate. The *Absconding Debtors Act*, for example, does not require a creditor seeking attachment to file a bond or undertaking for damages that the debtor might suffer as a result of a wrongful attachment. The Act contains no provision permitting a debtor to apply for a variation or modification of an order of attachment. The Commission believes that the present law does not provide a proper balance between the rights of creditors and the rights of debtors, and that this imbalance must be remedied.

As should be apparent from our comments, we believe that provisional relief should continue to play a role in the law of enforcement. However, we believe that the law of provisional relief in this Province should be put on a sound and rational jurisprudential footing. Before identifying those circumstances in which prejudgment relief should be available and outlining the safeguards necessary to prevent abuse in this area of the law, we turn to a discussion of prejudgment relief legislation and proposals for reform in other jurisdictions.

6. PREJUDGMENT RELIEF AND PROPOSALS FOR REFORM IN OTHER JURISDICTIONS

Prejudgment relief is one area of the law of enforcement in which there has been considerable activity in recent years. New attachment schemes have been introduced in Nova Scotia and Prince Edward Island during the 1970s.[348] At the same time, prejudgment measures of all sorts have come under attack by the courts in the United States, culminating in a series of decisions by the United States Supreme Court.[349] This judicial activity in turn has elicited a fresh legislative response to the subject.[350] Finally, there has been some examination of diverse prejudgment remedies in other jurisdictions, such as British Columbia, New Brunswick, and England.[351] In this section, we examine these recent developments.

(a) ATTACHMENT IN NOVA SCOTIA AND PRINCE EDWARD ISLAND

The 1971 revision of the Nova Scotia Civil Procedure Rules and Related Rules resulted, *inter alia*, in the introduction of the most comprehensive attachment law in Canada. The attachment provisions of the Nova Scotia Rules were adopted with only minor changes by Prince Edward Island in 1977. The discussion that follows focuses on the Nova Scotia Rules concerned with attachment.[352]

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[348] See discussion *infra*, sec. 6(a).

[349] See discussion *infra*, sec. 6(b)(i).

[350] See discussion *infra*, sec. 6(b)(ii).

[351] See discussion *infra*, secs. 6(c) and 6(d).

[352] The discussion that follows makes specific reference only to the Nova Scotia Rules. The attachment provisions in the Prince Edward Island Rules are virtually identical to the Nova Scotia attachment rules.

The provision governing attachment in the Nova Scotia Rules is Rule 49.01(1). It sets out the circumstances in which prejudgment attachment is available, and states as follows:

> 49.01.-(1) Where a defendant,
>
> (a) resides out of the jurisdiction, or is a corporation that is not registered under the Corporations Registration Act;
>
> (b) conceals himself or absconds within the jurisdiction with intent to avoid service on him of any document;
>
> (c) is about to leave or has left the jurisdiction with intent to change his domicile, defraud his creditors, or avoid service of a document;
>
> (d) is about to remove or has removed his property or any part thereof permanently out the jurisdiction;
>
> (e) has concealed, removed, assigned, transferred, conveyed, converted or otherwise disposed of all or any part of his property with intent to hinder or delay his creditors, or is about to do so;
>
> (f) has fraudulently incurred a debt or liability in issue in a proceeding;
>
> a plaintiff may, at or after the commencement of the proceeding and before judgment and as an incident of the relief claimed, make application for an attachment order . . . .

The scope of Rule 49.01(1) obviously is much broader than section 2(1) of the Ontario *Absconding Debtors Act*, which restricts attachment to cases where the debtor has departed from the jurisdiction with the intent to defraud his creditors or to avoid being arrested or served with process. The most important paragraphs of the Nova Scotia Rule are undoubtedly paragraphs (a), (d), and (e). By virtue of paragraph (a), a creditor is authorized to attach property of his debtor simply because he is a "non-resident". Paragraphs (d) and (e) are concerned with suspicious dealings by the debtor with his property. All the grounds for attachment specified in Rule 49.01(1) (some more than others) would appear to be consistent with the philosophy that a creditor should be able to claim security for the satisfaction of a future judgment in circumstances where there is some reason to believe that the debtor may try to deprive him of the fruits of his victory.

The other jurisdictional restrictions of Ontario's *Absconding Debtors Act* are not to be found in the Nova Scotia attachment provisions. The debtor need not be a person resident in Nova Scotia.[353] Nor is attachment under the Nova Scotia Rules restricted to situations where the debtor is "indebted" to the plaintiff.[354] It would appear that any cause of action, whether it be based, for example, on debt or a claim for damages arising out of the defendant's alleged tortious conduct, will support an application for an attachment order.

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[353] See discussion *supra*, sec. 2(b)(i)c.(3).

[354] *Ibid.*

It should be noted that, under the Nova Scotia Rules, a creditor may secure an attachment order only "at or after the commencement of the proceeding".[355] As will be recalled, by virtue of section 2(2) of the Ontario *Absconding Debtors Act*, an attachment order may be made "only in a pending action".

Besides the expanded jurisdictional bases for prejudgment attachment, the other major difference between the Nova Scotia Rules and Ontario's absconding debtors legislation is the important additional procedural safeguards included in the former. For instance, the supporting affidavit that must be filed by a Rule 49 applicant must state not only the nature of his cause of action, but sufficient facts to show that he has "a good cause of action against the defendant whose property is to be attached".[356] The affidavit also must contain a statement of the amount to which the creditor claims to be entitled, "after allowing for all just credits, set-offs and counterclaims known to him".[357] In this way, a creditor who succeeds in obtaining an attachment order will be able to tie up only so much of the debtor's property as will be needed to satisfy his ultimate judgment.

In addition to the supporting affidavit prescribed by Rule 49.02, an attaching creditor must submit a bond "in an amount equal to one and one quarter times the value of the property sought to be attached which the plaintiff seeks to recover . . . as stated in the plaintiff's affidavit, with two sufficient sureties, who shall justify, or other form of sufficient security".[358] Rule 49.03(2) describes the conditions of the bond:

> 49.03.-(2) Unless the court otherwise orders, the conditions of the bond shall be that,
>
> (a) the plaintiff shall prosecute the proceeding without delay to judgment; and
>
> (b) when ordered by the court,
>
> (i) the sheriff shall return the attached property, or the proceeds thereof if sold under rule 49.09, to the defendant or other person from whom it was attached, and
>
> (ii) the plaintiff shall pay to the defendant or other person the damages and costs that either of them has sustained by reason of the wrongful issue of the attachment order, or the wrongful making

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[355] R. 49.01(1).

[356] R. 49.02(a)(i).

[357] R. 49.02(b).

[358] R. 49.03(1).

> of any attachment thereunder, or if the plaintiff fails to recover judgment against the defendant in the proceeding, or as the court may order.

The Rules also contain provisions with respect to the circumstances in which a court may order another bond or further security to be given.[359]

Whereas an application for an order of attachment under Ontario's *Absconding Debtors Act* must be heard by a judge,[360] attachment in Nova Scotia is within the purview of a prothonotary, a clerk of the court.[361] The court has simply a supervisory role in the issuance of attachment orders. While this aspect of the Nova Scotia scheme of attachment may result in more expeditious prejudgment relief, one may wonder whether a court clerk is in the best position to determine, for example, whether the creditor has "a good cause of action against the debtor".

Pursuant to Rule 49.04(1)(a), the sheriff to whom an attachment order is delivered is required, within ninety days or within such further time as the court orders, to attach sufficient of the debtor's property "as will secure in whole or in part the amount of the claim which the plaintiff seeks to recover from the [debtor] as stated in the attachment order". The sheriff, by virtue of this Rule, is authorized to attach "*any property* in which the debtor has an interest, including any debt, rent, legacy, share, bond, debenture or other security, currency or other demand, due or accruing due at any time while the order is valid".[362] Like section 7 of the Ontario *Absconding Debtors Act*, Rule 49.04(1)(a) empowers the sheriff to take only property "not exempt by law from seizure".

Generally speaking, the Nova Scotia Rules do not specify the manner in which attachment is to be effected. However, in the case of property in the possession of a third person, Rule 49.04(1)(f) provides that such property is deemed to have been attached upon service of an attachment order upon the third person. Special provision also is made for the attachment of real property and shares, bonds, debentures, or other interests of a debtor in a corporation. Real property is deemed to be attached by serving the occupants of the property with a copy of the attachment order and by registering another copy in the proper registration district.[363] If the property is not occupied, Rule 49.04(1)(g) allows a copy of the order to be posted in a conspicuous place on the property. Insofar as shares and other interests of a debtor in a corporation are concerned, Rule 49.07(1) states that attachment may be effected "by serving the attachment order upon the body corporate".

Where no particular method of attachment is specified by the Nova Scotia Rules, it is clear that the sheriff need not take the property into his possession to effect its attachment. Indeed, unless instructed by the attaching creditor to remove the property, Rule 49.04(1)(e)(i) requires the sheriff "to leave the property in the place where it was attached in the custody of the defendant or person in whose possession it had been at the time of attachment".

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[359] R. 49.03(3).

[360] *Supra*, note 44, s. 3(1).

[361] R. 49.01(2).

[362] Emphasis added.

[363] R. 49.04(1)(g).

Although property that has been attached may be sold in certain circumstances, the sheriff's primary obligation is "to hold and safely keep any property attached . . . to satisfy any execution order issued to enforce any order obtained against a defendant".[364] There are four circumstances, including sale of the property, in which the sheriff's primary obligation is lifted.

First, the creditor may authorize the sheriff to return the attached property.[365] Secondly, the debtor, by filing a bond, becomes entitled to regain possession of the attached property.[366] Under Rule 49.06(2), the court is given broad discretionary powers regarding the conditions of the debtor's bond.

As we have mentioned already, sale of the attached property may be ordered in appropriate circumstances. Rule 49.09(1) provides as follows:

> 49.09.-(1) When any attached personal property is likely to perish or materially depreciate in value before the probable termination of the proceeding, or the keeping of the property could result in unreasonable loss or expense, or for other just cause, the court may order the sale or other disposal of all or any part of the property in such manner and upon such terms as are just.

It should be noted that a court may authorize the sale of only personal property under this Rule. Once again, the courts are given a broad discretion, since sale may be ordered for any just cause, and upon such terms as seem just.

The final circumstance in which the sheriff is relieved of his primary obligation under the Nova Scotia attachment provisions is where an attachment order is set aside by a court.[367] Rule 49.10(2) enables both the debtor and any other person claiming an interest in the property to challenge an attachment order and to ask that the order be overturned. In addition to the power to set aside an attachment order, the courts, under Rule 49.12(b) and (c) respectively, are empowered to "amend or modify" the order or, in appropriate circumstances, to "vacate or dissolve in whole or in part" any order.[368] In both cases, a court also may order the return of

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[364] R. 49.05(2).

[365] R. 49.05(2)(b).

[366] R. 49.05(2)(a).

[367] R. 49.05(2)(d).

[368] R. 49.12 reads in part as follows:

> 49.12. When an attachment order has been granted, the court may on notice,
>
> . . . .
>
> (c) upon being satisfied that the attachment order is not necessary for the security of a plaintiff, or a plaintiff has failed to bring the proceeding to trial and judgment promptly, or the proceeding has been discontinued or dismissed

any property that was attached under the order.[369]

Before leaving the Nova Scotia attachment rules, one other provision should be mentioned briefly. Rule 49.12(a) provides as follows:

> 49.12. When an attachment order has been granted, the court may on notice,
>
> (a) grant a plaintiff a reasonable opportunity to amend any affidavit or bond used in support of the grant of an attachment order; . . .

This Rule was introduced, it would seem, to overcome the strict constructionist approach that has been the hallmark of judicial treatment of prejudgment relief legislation in Canada.

(b) ATTACHMENT IN THE UNITED STATES

It was in the American colonies that the custom of foreign attachment really took root and developed.[370] From the middle of the nineteenth century to the late 1960s, the attachment laws of most states remained basically unchanged. In the last decade, however, there has been something of a revolution in the law of attachment in the United States, particularly in its procedural aspects. The force behind the recent changes in the law has been a series of four decisions by the Supreme Court of the United States concerned with the constitutionality of certain kinds of prejudgment relief. In this section, we shall look at these decisions and their impact on prejudgment attachment legislation in California, Michigan, and New York.

(i) Prejudgment Relief and Due Process

Until 1969, few people in the United States doubted that prejudgment garnishment legislation was constitutionally valid: the matter, it would seem, had been put to rest by a number of decisions of the United States Supreme Court, including *McKay v. McInnes*,[371] decided in 1929. The Supreme Court's decision in *Sniadach v. Family Finance Corp. of Bay View*[372] in 1969 upset this state of affairs.

The Court in *Sniadach* concluded that Wisconsin's prejudgment garnishment legislation contravened the due process clause of the United States Constitution.[373] The basis of the Court's decision would seem to

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> as against a defendant, or a plaintiff's claim against a defendant has been fully satisfied, or for other just cause, vacate or dissolve in whole or in part, the attachment order and any attachment made thereunder; . . .

[369] See r. 49.12(d).

[370] For a brief discussion of foreign attachment, see *supra*, sec. 2(b)(i)a.

[371] 279 U.S. 820, 49 S. Ct. 344 (1929).

[372] *Sniadach v. Family Finance Corp. of Bay View*, 395 U.S. 337, 89 S. Ct. 1820 (1969) (subsequent references are to 89 S. Ct.).

[373] Section 1 of the 14th Amendment of the U.S. Constitution provides as follows:

> All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive

have been that prejudgment garnishment of the debtor's wages was available without any requirement that the debtor be given prior notice of the proceedings or an opportunity to be heard prior to the relief being granted. The Court was influenced greatly by the fact that the debt in question, wages, was "a specialized type of property presenting distinct problems".[374] In his judgment, Mr. Justice Douglas noted that the garnishment of wages before judgment could cause the debtor "tremendous hardship".[375] The creditor in turn would be able in many cases to gain great leverage over the debtor in respect of the resolution of the main dispute, with the result that a wage-earning family could be driven "to the wall".[376]

In 1972, in *Fuentes v. Shevin*,[377] the Supreme Court ruled that Florida and Pennsylvania's replevin statutes were unconstitutional. Again, the focus of discussion in the judgment of the Court, delivered by Mr. Justice Stewart, was the lack of procedural due process in proceedings under the challenged legislation. Mr. Justice Stewart concluded that the due process guarantees of the United States Constitution could be satisfied only if notice and a hearing were granted "at a time when . . . deprivation can still be prevented".[378]

In arriving at this conclusion, Mr. Justice Stewart rejected the argument that the right to secure the release of replevied property by the posting of a bond was a satisfactory substitute for a prior hearing. While the existence of such a safeguard, and the length and severity of the deprivation, might be factors to be weighed in determining the type of hearing that must be provided, these factors did not obviate the need for a prior hearing. He dismissed the arguments that the right to be heard should be dependent on one's chances of success in the main dispute and that the *Sniadach* doctrine should be restricted to property that can be characterized as necessaries, stating "if the root principle of procedural due process is to be applied with objectivity, it cannot rest on such distinctions".[379]

> any person of life, liberty, or property *without due process of law*; nor deny to any person within its jurisdiction the equal protection of the laws. [Emphasis added.]

While the recently enacted *Canadian Charter of Rights and Freedoms* contains what may be called a "due process clause", section 7 of the Charter does not provide express protection for property rights. Section 7 provides as follows:

> 7. Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice.

At least one court has found that the words "security of the person" may be sufficiently broad to provide constitutional protection for property rights: see *The Queen in right of New Brunswick v. Fisherman's Wharf Ltd.* (1982), 40 N.B.R. (2d) 42, 135 D.L.R. (3d) 307 (Q.B.), aff'd on appeal for other reasons, unreported (December 31, 1982, N.B.C.A.).

[374] *Supra*, note 372, at 1822.

[375] *Ibid.*

[376] *Ibid.*, at 1823.

[377] 407 U.S. 67, 92 S. Ct. 1983 (1972) (subsequent references are to 92 S. Ct.).

[378] *Ibid.*, at 1994.

[379] *Ibid.*, at 1999.

Shortly after it enunciated the "prior hearing" requirement, the United States Supreme Court began to back away from a mandatory prior hearing in all cases of provisional relief and to adopt a much more flexible approach to procedural due process. At issue in *Mitchell v. W.T. Grant Co.*,[380] the third Supreme Court decision, was the constitutionality of Louisiana's sequestration procedure, which was available to a mortgagee or lienholder to prevent the wasting or alienation of encumbered property.

In *Mitchell*, the Court moved toward a balancing of interests approach. Whether notice and a prior hearing were necessary in any given case would depend upon the other procedural safeguards present in the challenged legislation, and the interests of the parties to be protected. In upholding the Louisiana legislation, Mr. Justice White, who delivered the majority judgment in *Mitchell*, pointed out that both the creditor and the debtor had an interest in the sequestered property. He also pointed out that, under the Louisiana legislation, the debtor had a right to seek an immediate dissolution of the writ of sequestration, and a right to secure the return of his property by the posting of a bond. These and other statutory provisions, he concluded, resulted in a "constitutional accommodation of the conflicting interests of the parties"[381] that obviated the need for notice and a hearing prior to the granting of the requested relief.

In the last of this series of four decisions respecting provisional relief and due process, *North Georgia Finishing, Inc. v. Di-Chem, Inc.*,[382] the United States Supreme Court seemed to waver between the position advocated by Mr. Justice Stewart in *Fuentes* and that urged by Mr. Justice White in *Mitchell*. Neither of the tests set out in these two decisions was met by the Georgia prejudgment garnishment legislation under attack in this case. However, the fact that the Court considered whether sufficient *Mitchell* safeguards were present in the statute would suggest that notice and an opportunity to be heard prior to the granting of prejudgment relief are not necessary in every case. Rather, it appears that the court will consider on a case-by-case basis whether, given the interests of the parties to the dispute, the legislation in question contains sufficient procedural safeguards to ensure that no person will be deprived of his property without due process of law.

(ii) The Legislative Response

In response to *Sniadach* and its progeny, the prejudgment attachment legislation of California, Michigan, and New York was substantially amended. In each jurisdiction, a different legislative approach was adopted.

a. California

Since 1972, California's prejudgment attachment legislation has been greatly amended. An interim attachment law was enacted in that year,[383] while the matter of prejudgment attachment was reviewed by the California Law Revision Commission. The Commission submitted recommendations for reform in 1973,[384] and again in 1975,[385] and most of these recommendations now have received legislative approval.[386]

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[380] 416 U.S. 600, 94 S. Ct. 1895 (1974) (subsequent references are to 94 S. Ct.).

[381] *Ibid.*, at 1900.

[382] 419 U.S. 601, 95 S. Ct. 719 (1975).

[383] Cal. Stats. 1972, c. 550.

The scope of California's new attachment legislation was influenced not only by the pronouncements of the United States Supreme Court in *Sniadach v. Family Finance Corp. of Bay View*, but also by the decision of the Supreme Court of California in *Randone v. Appellate Dept. of the Superior Court*.[387] There the Court found that California's prejudgment attachment legislation was unconstitutional for the reasons expressed in *Sniadach*, but also because it allowed the attachment of the "necessities of life" without notice and an opportunity to be heard. The Supreme Court of California was of the view that "the hardship imposed on a debtor by the attachment of his 'necessities of life' is so severe that we do not believe that a creditor's private interest is ever sufficient to permit the imposition of such deprivation before notice and a hearing on the validity of the creditor's claim".[388] The California legislature sought to cure both of the deficiencies in its prejudgment attachment law pointed out by the Supreme Court of California.

Insofar as necessities of life are concerned, legislation enacted since 1972 has sought to prevent the prejudgment attachment of such property in a number of different ways. First, in addition to prohibiting the attachment of property exempt from execution, section 487.020(b) of the California Code of Civil Procedure exempts from attachment "[p]roperty which is necessary for the support of an individual defendant or the defendant's family supported in whole or in part by the defendant". Wages too are exempt from attachment.[389]

Secondly, prejudgment attachment has been restricted in a number of important ways that may have an impact upon the attachment of necessities. Attachment now is available only in respect of claims for money equal to or in excess of $500.[390] Attachment in the case of an individual debtor "may be issued only on a claim which arises out of the conduct by the individual of a trade, business, or profession".[391] In addition, claims against an individual based, *inter alia*, on the sale or lease of property or the furnishing of services will support attachment proceedings only if the property or services is not used by the individual primarily for personal, family, or household purposes.[392] By the two latter restrictions it was thought that attachment against individuals could be reduced substantially, with a concomitant reduction in the likelihood that necessities would be attached.[393]

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[384] California Law Revision Commission, "Recommendation Relating to Prejudgment Attachment", in 11 Cal. L. Revision Comm'n Reports (1973) 701.

[385] California Law Revision Commission, "Recommendation Relating to the Revision of the Attachment Law", in 13 Cal. L. Revision Comm'n Reports (1975) 801.

[386] See Cal. Stats. 1974, c. 1516, and Cal. Stats. 1975, c. 200. The legislation was recently amended by Cal. Stats. 1982, c. 1198, which is to come into force on July 1, 1983. The discussion in this Report is based on the law as of March 31, 1983.

[387] 96 Cal. Rptr. 709, 488 P.2d 13 (1971) (subsequent reference is to 488 P.2d).

[388] *Ibid.*, at 27.

[389] West's Cal. Code Civ. Pro. (1982), §487.020(c).

[390] *Ibid.*, §483.010(a).

[391] *Ibid.*, §483.010(c).

In addition to enacting provisions relating to necessities, California has moved away from attachment without notice, and has introduced a noticed hearing procedure.[394] While, under section 485.010 of the California Code of Civil Procedure, a creditor still may obtain a writ of attachment in *ex parte* proceedings, this right has been circumscribed severely. Only if "it appears from facts shown by affidavit that great or irreparable injury would result . . . if issuance . . . were delayed until the matter could be heard on notice"[395] will a writ of attachment issue in *ex parte* proceedings. Under similar circumstances, the creditor also may be able to obtain a "temporary protective order" without having to give the debtor notice of the application.[396] Irrespective of the procedure adopted by the creditor, he now is required to establish the probable validity of his claim before a writ of attachment or a temporary protective order will be granted.[397]

The present California attachment legislation contains other procedural safeguards as well. For example, both prejudgment attachment and the issuance of temporary protective orders are matters that must go before a court: judicial supervision is a *sine qua non* of such prejudgment relief. Section 489.210 provides that "[b]efore issuance of a writ of attachment or a temporary protective order, the [creditor] shall file an undertaking to pay the defendant any amount the defendant may recover for any wrongful attachment". The debtor may secure the release of any attached property by applying to the court for an order "permitting the defendant to substitute an undertaking for any of his property".[398]

b. Michigan

Michigan legislators have taken a radically different approach from that adopted by California legislators to the problems raised by *Sniadach* and the other decisions of the Supreme Court of the United States discussed earlier.

In 1972, shortly after the Supreme Court's decision in *Fuentes*, the Michigan Law Revision Commission released its "Recommendations Relating to Due Process in Seizure of a Debtor's Property". After reviewing the Supreme Court decisions in *Sniadach* and *Fuentes*, the Commission commented as follows:[399]

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[392] *Ibid.*

[393] See *supra*, note 384, at 721-23.

[394] West's Cal. Code Civ. Pro. (1982), §§484.010 *et seq*.

[395] *Ibid.*, §485.010(a).

[396] *Ibid.*, §§486.010-486.110. A temporary protective order is akin to a prejudgment injunction restraining the debtor from disposing of his property.

[397] *Ibid.*, §§484.090(a)(2), 485.220(a)(2), and 486.020(b).

[398] *Ibid.*, §489.310(a).

[399] Michigan Law Revision Commission, "Recommendations Relating to Due Process in Seizure of a Debtor's Property", in *7th Annual Report* (1972) 7, at 11.

> To conform prejudgment attachment and garnishment practice with the standards prescribed in the *Fuentes* and *Sniadach* opinions, Michigan statutes would have to be amended to provide for a noticed hearing at which the court would have to determine (1) the probable validity of the primary claim, and (2) the existence of the asserted statutory ground for issuing the writ. . . . The obvious judicial burden this would entail should be carefully weighed against the creditor's need for such a prejudgment remedy, as well as its basic unfairness to the debtor who has not yet had his day in court.

The Commission was of the opinion that prejudgment attachment and garnishment were simply methods by which a creditor could acquire "collateral security which he has not bargained for, on a claim which in advance of trial has never been proven".[400] Restricting these remedies to circumstances indicating possible fraudulent transfer or concealment of assets did not, in the Commission's view, meet the argument that they could be used to put pressure on a debtor to settle the creditor's claim at an early stage and on terms favourable to the creditor.

For the abovementioned reasons, the Michigan Law Revision Commission recommended the abolition of prejudgment attachment and garnishment, except as a basis for claiming jurisdiction or, in other words, as a means of foreign attachment.[401] The Commission's recommendations became law in 1974.[402]

Only four years later, in 1978, the Michigan Law Revision Commission looked at foreign attachment in the light of the decision in *Shaffer v. Heitner*,[403] where it was decided that a claim of jurisdiction based solely on the ownership and attachment of intangibles in the jurisdiction was unconstitutional. The Commission concluded that it was time that prejudgment attachment and garnishment were abolished entirely so that the rights of a creditor would be no greater in a case of a nonresident than in the case of a resident defendant.[404]

c. *New York*

As in the case of California and Michigan, the prejudgment attachment provisions of the New York Civil Practice Law and Rules[405] have had to be amended to conform with the pronouncements of the United States Supreme Court regarding the constitutionality of prejudgment relief legislation. The changes in the New York legislation have been restricted in the main to two areas: the grounds for attachment and the procedural safeguards to protect debtors from abusive use of prejudgment attachment.

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[400] *Ibid.*, at 12.

[401] *Ibid.*, at 13.

[402] P.A. 1974, No. 371.

[403] *Shaffer v. Heitner*, 433 U.S. 186 (1977).

[404] Michigan Law Revision Commission, *13th Annual Report* (1978), at 22. For a recent decision of the United States Supreme Court questioning the constitutional propriety of assuming jurisdiction on the ground of foreign attachment, see *Rush v. Savchuk*, 444 U.S. 320 (1980).

[405] N.Y. Civ. Prac. Law (McKinney).

Regarding the grounds for attachment, section 6201 of the New York Civil Practice Law and Rules now provides as follows:

> 6201. An order of attachment may be granted in any action, except a matrimonial action, where the plaintiff has demanded and would be entitled, in whole or in part, or in the alternative, to a money judgment against one or more defendants, when:
>
> 1. the defendant is a nondomiciliary residing without the state, or is a foreign corporation not qualified to do business in the state; or
>
> 2. the defendant resides or is domiciled in the state and cannot be personally served despite diligent efforts to do so; or
>
> 3. the defendant, with intent to defraud his creditors or frustrate the enforcement of a judgment that might be rendered in plaintiff's favor, has assigned, disposed of, encumbered or secreted property, or removed it from the state or is about to do any of these acts; or
>
> 4. the cause of action is based on a judgment, decree or order of a court of the United States or of any other court which is entitled to full faith and credit in this state, or on a judgment which qualifies for recognition under the provisions of article 53.

Abolished as grounds for attachment in 1977 were the following:

> (i) the defendant, with intent to defraud his creditors or to avoid the service of summons, has departed or is about to depart from the state, or keeps himself concealed therein; or
>
> (ii) the defendant, in an action upon a contract, express or implied, has been guilty of a fraud in contracting or incurring the liability; or
>
> (iii) the action is based upon the wrongful receipt, conversion or retention, or the aiding or abetting thereof, of any property held or owned by any governmental agency, including a municipal or public corporation, or officer thereof; or
>
> (iv) there is a cause of action to recover damages for the conversion of personal property, or for fraud or deceit.

In short, the New York legislators have tried to restrict the availability of attachment to cases where it is necessary for jurisdiction, or where the debtor has dealt with his property to the detriment of his creditors.

The major procedural change in New York's attachment provisions is the introduction of a noticed hearing procedure.[406] Use of this procedure is, however, optional: in all cases a creditor still may apply for attachment

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[406] N.Y. Civ. Prac. Law §6210 (McKinney). To minimize the risk entailed in giving the debtor notice of an application for attachment, this section also allows a creditor to obtain, "without notice to the defendant, . . . a temporary restraining order prohibiting the transfer of assets".

ex parte.[407] But where the latter procedure is used, the creditor must now apply for an order confirming the *ex parte* order of attachment. This application is required to be brought "within a period not to exceed five days after levy" and must be "on such notice as the court shall direct".[408] To provide the debtor with additional protection, the creditor must satisfy the court on such a motion of "the grounds for the attachment, the need for the continuing levy and the probability that he will succeed on the merits".[409]

(c) PROPOSALS FOR REFORM: THE CANADIAN SCENE

To date, reform of the laws affecting provisional relief has attracted very little attention in Canada. While there have been recent changes to the law of attachment in Nova Scotia and Prince Edward Island,[410] the only other jurisdictions that have reviewed some of the prejudgment remedies now available are British Columbia and New Brunswick. The following is a brief outline of reform efforts in these two jurisdictions.

(i) British Columbia

In 1978, as part of its review of the law of debtor-creditor relations, the Law Reform Commission of British Columbia examined and recommended the repeal of that Province's *Absconding Debtors Act*.[411] The British Columbia Act, it should be noted, was based on Upper Canada's early absconding debtors legislation.[412]

In its *Report on The Absconding Debtors Act and Bail Act: Two Obsolete Acts*,[413] the Commission gave two main reasons for repeal of the *Absconding Debtors Act*. First, it was of the view that this legislation gave rise to "very onerous evidentiary requirements",[414] with the result that the

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[407] *Ibid.*, §6211(a).

[408] *Ibid.*, §6211(b).

[409] *Ibid.*, §6223(b).

[410] For a discussion of the attachment rules in Nova Scotia and Prince Edward Island, see *supra*, sec. 6(a).

[411] R.S.B.C. 1960, c. 1. Compare Law Reform Commission of Western Australia, *Report on the Absconding Debtors Act 1877-1965* (1981) (hereinafter referred to as the "Western Australia Report"), where the modernization of absconding debtors legislation was proposed. It should be noted that the existing legislation in Western Australia provides only for the arrest of absconding debtors. The Law Reform Commission of Western Australia recommended not only that prejudgment arrest of absconding debtors should continue to be available, but it also proposed that a creditor should be able to apply to the court for an order restraining the debtor from transferring his property or removing it from the jurisdiction: *ibid.*, para. 7.17, at 47.

[412] See *The Common Law Procedure Act*, 19 Vict., c. 43 (U.C.).

[413] Law Reform Commission of British Columbia, *Report on The Absconding Debtors Act and Bail Act: Two Obsolete Acts* (1978) (hereinafter referred to as the "British Columbia Report").

[414] *Ibid.*, at 7. The utility of the Act, the Commission pointed out, also had been affected by the existence of liberal service *ex juris* rules in British Columbia that allowed a creditor "simply to commence an ordinary action against an absconding debtor, take judgment in the usual way and execute against the property the debtor has left behind in the Province": see *ibid.*, at 6-7.

Act seemed to have been invoked but rarely. However, the Commission did not believe that the evidentiary inadequacies of the Act alone justified repeal.

Of far greater concern to the Commission was the fact that the *Absconding Debtors Act* gave rise to a serious anomaly. While the Act could be used to attach the property of a debtor who had left the jurisdiction, it could not be called upon by a creditor whose debtor was about to depart from the jurisdiction with the necessary intent. The British Columbia Law Reform Commission found the historical basis for this distinction less than compelling:[415]

> In 1832 imprisonment for debt was an important creditors' remedy and was widely used. It was open to a creditor, in an appropriate case, to issue a writ of *capias ad respondendum* as originating process in his action. This writ directed the sheriff to arrest the defendant who would then secure his release by giving security, in the form of civil bail, for both his appearance in the action and for any resulting judgment. This procedure, sometimes referred to as 'arrest on mesne process', was, of course, not available to a creditor where his debtor had fled the jurisdiction and the *Absconding Debtors Act* seems designed to assist that creditor by creating a new remedy to replace the one lost.
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> At the time the Act was developed, to limit the availability of this prejudgment remedy against property to the creditor whose debtor had absconded may have been justifiable. Other creditors had a prejudgment remedy against the person. But the latter process has long been unavailable. Today arrest on mesne process for debt is regarded as unacceptable and has been abolished. However, abolishing *capias ad respondendum* as originating process while retaining the *Absconding Debtors Act* yields the anomalous result that the creditor whose debtor has absconded is in a more favourable legal position than the creditor whose debtor has remained in the jurisdiction. In our view this distinction cannot be allowed to stand.

Although it recommended the repeal of the *Absconding Debtors Act*, the British Columbia Commission did suggest that provisional relief might be justified under certain circumstances. Indeed, the Commission recognized "that in many cases creditors and potential litigants may have a legitimate need for the protection that prejudgment process can offer",[416] and indicated that this matter was under consideration by the Commission. In conclusion, the 1978 Report stated as follows:[417]

> One thing that is clear . . . is that the *Absconding Debtors Act* does not provide an appropriate legal framework for a more general prejudgment remedy. It is over 150 years old in concept; its language and substance are directed to a society and a legal regime that ceased to exist many years ago; and it adopts unacceptable criteria for the granting of relief.

The *Absconding Debtors Act* was repealed in 1978.[418]

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[415] *Ibid.*, at 8.

[416] *Ibid.*

[417] *Ibid.*

[418] *Attorney-General Statutes Amendment Act, 1978*, S.B.C. 1978, c. 11, s. 1.

The other prejudgment remedy that has received attention from the Law Reform Commission of British Columbia is prejudgment arrest of a debtor. In its *Report on The Absconding Debtors Act and Bail Act: Two Obsolete Acts*, the Commission noted the trend toward the abolition of arrest as a prejudgment remedy. Consistent with the repeal of the *Arrest and Imprisonment for Debt Act*[419] and the abolition of bail in alimony proceedings, it proposed that the *Bail Act*[420] be repealed,[421] and this has since been done.[422]

(ii) New Brunswick

Both the New Brunswick *Absconding Debtors Act*[423] and *Arrest and Examinations Act*[424] were reviewed in 1976 by the Law Reform Division of the New Brunswick Department of Justice in Volume II of its *Third Report of the Consumer Protection Project* concerned with the legal remedies of the unsecured creditor after judgment.[425]

The New Brunswick *Absconding Debtors Act* differs substantially from its Ontario counterpart. As the New Brunswick Report stated, the Act is "unique in Canada in providing under provincial legislation for what is in effect an involuntary assignment for the benefit of [the debtor's] creditors".[426] It would appear that, under the New Brunswick Act, all the debtor's property would be subject to attachment, not just property sufficient to satisfy the attaching creditor's claim. This view would seem to be strengthened by section 13 of the Act, which states that "from the time of the issuing of such absconding debtor's warrant, the *estate* of the debtor shall vest in the sheriff for the benefit of the creditors of the debtor to the same extent as if the warrant had been an assignment by the debtor . . . under the provisions of the *Assignments and Preferences Act*,[427] and the provisions of that Act apply to all proceedings hereunder . . .".[428]

Like the Law Reform Commission of British Columbia, the Law Reform Division of the New Brunswick Department of Justice recommended the repeal of the Province's existing absconding debtors provisions. Among the reasons given for arriving at this conclusion were the following:[429]

> They provide an unnecessary short-cut for creditors to avoid the normal procedure to judgment. To a large extent they provide execution without judg-

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[419] R.S.B.C. 1960, c. 17, repealed by S.B.C. 1975, c. 4, s. 1.

[420] R.S.B.C. 1960, c. 23.

[421] British Columbia Report, *supra*, note 413, at 10. Compare Western Australia Report, *supra*, note 411.

[422] *Supra*, note 418, s. 2.

[423] R.S.N.B. 1973, c. A-2.

[424] R.S.N.B. 1973, c. A-12.

[425] New Brunswick Department of Justice, Law Reform Division, *Third Report of the Consumer Protection Project*, Vol. II, *Legal Remedies of the Unsecured Creditor After Judgment* (1976) (hereinafter referred to as the "New Brunswick Report").

[426] *Ibid.*, at 94.

[427] R.S.N.B. 1973, c. A-16.

[428] Emphasis added.

[429] New Brunswick Report, *supra*, note 425, at 95.

> ment, rather than execution before judgment. The latter may be acceptable where safeguards are provided to ensure that the plaintiff either obtains judgment or compensates the defendant, but execution without judgment is contrary to due process of law.

In its stead, the New Brunswick Report recommended that a procedure be provided "for an attachment of the defendant's property before judgment after the plaintiff has commenced a normal legal action where the defendant is absent or absconding from the province".[430] Some of the features recommended for inclusion in such a procedure were safeguards for the rights of the defendant in the event that the plaintiff did not obtain judgment, a method by which the defendant could obtain the release of his property by giving security, and exemptions from attachment similar to those available in the case of execution after judgment.[431] Finally, it was recommended that the proposed legislation also provide for the disposition of any attached property after judgment in accordance with "normal procedures for enforcing judgments".[432] Special provision could be made for the disposition of perishables.

Regarding prejudgment arrest of a debtor as a means of providing a creditor with provisional relief, the New Brunswick Report recommended the elimination of "all remaining provisions for arrest of a person in a civil action, before or after judgment, other than provisions for punishment of disobedience of a direct court order"[433] under the court's contempt power. The New Brunswick Report noted that arrest, by itself, hindered rather than assisted the process of collection.[434] Moreover, the Report concluded that "[t]he cost of imprisonment to the individual arrested and to society invariably outweighs the benefit to the claimant".[435]

(d) REPORT OF THE COMMITTEE ON THE ENFORCEMENT OF JUDGMENT DEBTS

Provisional relief is a matter that was also considered in England in the *Report of the Committee on the Enforcement of Judgment Debts*,[436] otherwise known as the Payne Committee Report.

As was mentioned earlier, until the advent of the *Mareva* injunction, an unsecured judgment creditor in England was unable to obtain effective provisional relief.[437] Of course, where the property in question was the subject matter of the litigation, a preservation order was available under the English equivalent[438] of Rule 372 of the Supreme Court of Ontario Rules of Practice.[439]

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[430] *Ibid.* (emphasis deleted).

[431] *Ibid.*

[432] *Ibid.* (emphasis deleted).

[433] *Ibid.*, at 78 (emphasis deleted). Compare Western Australia Report, *supra*, note 411.

[434] New Brunswick Report, *supra*, note 425, at 69.

[435] *Ibid.*, at 77.

[436] Payne Committee Report, *supra*, note 238.

[437] Prejudgment arrest, however, was available under s. 6 of the English *Debtors Act 1869*, 32 & 33 Vict., c. 62.

[438] Rules of the Supreme Court 1965, Ord. 29, r. 2.

[439] See discussion *supra*, sec. 2(a)(iv).

Having regard to "modern conditions of travel",[440] the Payne Committee concluded that existing English law was inadequate and recommended that the "court should have power before or after judgment to restrain a debtor from disposing of property or transferring it out of the jurisdiction, with the intention of defeating his creditors".[441] The Payne Committee went so far as to state that, in certain circumstances, a restraining order should be available even before the commencement of legal proceedings against the debtor.[442] However, it proposed that a restraining order should be granted before the institution of legal proceedings only on "terms that the writ or summons should be issued on the next day on which the court office is open".[443]

The Payne Committee recommended that, in order to obtain a restraining order, a creditor should be required to establish that he has a good cause of action against the debtor, that the debtor has property to meet a future judgment in whole or in part, and that there is probable cause to believe that his debtor "is about to dispose of the same, or transfer it out of the jurisdiction, or otherwise deal with the same so as to defeat the creditor's claim".[444] Finally, it was recommended that the power to grant such relief should be vested in judges of the superior courts.[445]

The final noteworthy recommendation in the Payne Committee Report respecting provisional relief concerns prejudgment arrest. The Payne Committee was of the view that the introduction of a power to issue a prejudgment restraining order obviated the need for any prejudgment arrest power. Accordingly, it recommended that the prejudgment arrest power found in section 6 of the English *Debtors Act 1869*[446] should be repealed,[447] and that the writ of *ne exeat regno* also should be abolished.[448]

7. THE NEW LAW OF PROVISIONAL RELIEF

Previously in this chapter, we concluded that prejudgment relief should continue to be available to creditors in Ontario. However, we also recognized the need to put the law in this area on a sound and rational footing. Accordingly, we now turn to consider the kind of provisional relief that a creditor in Ontario should be entitled to claim, the circumstances under which such relief should be granted, and the protection that should be afforded to a debtor who may be subject to prejudgment relief. We begin with a brief description of the kind of provisional relief that we believe should be available.

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[440] Payne Committee Report, *supra*, note 238, para. 1252, at 324.

[441] *Ibid.*, para. 1260, at 325. As a precedent for this proposal, the Payne Committee pointed to the availability of restraining orders under s. 32 of the English *Matrimonial Causes Act 1965*, c. 72. See now the *Matrimonial Proceedings and Property Act 1970*, c. 45, s. 16.

[442] Payne Committee Report, *supra*, note 238, para. 1254, at 324.

[443] *Ibid.*, para. 1255(iv), at 325.

[444] *Ibid.*, para. 1255, at 324-25. The conditions that must be satisfied to obtain a *Mareva* injunction are strikingly similar to those proposed by the Payne Committee Report: see discussion *supra*, sec. 3(a).

[445] *Ibid.*

[446] *Supra*, note 437. Insofar as the postjudgment arrest provisions of this Act are concerned, see Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

[447] Payne Committee Report, *supra*, note 238, para. 1260, at 326.

[448] *Ibid.* The writ of *ne exeat regno* is the equitable equivalent of the writ of *capias ad respondendum*.

(a) A REMEDY AGAINST THE DEBTOR'S PROPERTY VERSUS ARREST OF HIS PERSON

The purpose of prejudgment relief, in our view, should be to provide a creditor in appropriate circumstances with security for the payment of a future judgment against the debtor. As we have seen, this objective can be achieved in two ways: the "taking" of the debtor's property as security, or arrest of the debtor himself. The Commission believes that, generally speaking, the debtor's property will provide his creditor with the necessary security, in a more effective and equitable manner than prejudgment arrest.

It is argued that the arrest of a debtor before judgment has been rendered against him can effect the desired security function indirectly at best, forcing the debtor to provide his creditor with adequate security. Where the debtor does not have the means to give such security, his arrest will have been for naught. Where the debtor does have the means, it seems much more sensible to do directly what arrest can do only indirectly – and at a cost "to the individual arrested and to society [that] invariably outweighs the benefit to the claimant".[449]

In addition, with the introduction of the *Canadian Charter of Rights and Freedoms*,[450] there may be some question regarding the constitutional validity of existing prejudgment arrest legislation. Section 7 of the Charter provides that "[e]veryone has the right to . . . liberty and the security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice". Any law inconsistent with the Charter is, by virtue of section 52 of the *Constitution Act, 1982*,[451] rendered of no force or effect. It is suggested that, at a minimum, in order to comply with section 7 of the *Charter of Rights and Freedoms*, prejudgment arrest legislation would have to provide the debtor with an opportunity to be heard prior to his arrest, or immediately upon his arrest.[452]

We already have noted the repeal of prejudgment arrest legislation in British Columbia in recent years, and the call for the abolition of this remedy in New Brunswick and England in the last decade or so.[453] On balance, the Commission has concluded that, except in the family law context, prejudgment arrest of debtors should be abolished: a creditor should be able to look only to his debtor's property for provisional relief. Accordingly, we recommend that the provisions of the *Fraudulent Debtors Arrest Act*[454] concerned with prejudgment arrest should be repealed.

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[449] New Brunswick Report, *supra*, note 425, at 77.

[450] Being Part I of the *Constitution Act, 1982*, which itself is scheduled to the *Canada Act 1982*, c. 11 (U.K.), proclaimed in force on April 17, 1982.

[451] *Ibid.*

[452] See the discussion of the impact of the due process Amendments of the U.S. Constitution on prejudgment remedies *supra*, sec. 6(b)(i).

[453] See *supra*, secs. 6(c) and (d).

This recommendation would leave section 24 of the *Family Law Reform Act* untouched. In our view, section 24 of the *Family Law Reform Act* – authorizing the prejudgment arrest of a respondent to an application for support where the court is satisfied that he or she is about to leave Ontario – should not be repealed. We believe that, given the nature of the claim, a full range of remedies ought to be available to an applicant for support. Nevertheless, because of the enactment of the *Canadian Charter of Rights and Freedoms*, the Commission is of the opinion that section 24 must be amended to ensure that the rights and freedoms of the debtor are adequately safeguarded.[455] To this end, we recommend that section 24 of the *Family Law Reform Act* should be retained but that, insofar as it authorizes prejudgment arrest, the section should be amended to require that the debtor be brought before the court as soon as possible after his arrest to show cause why he should not be detained. At this time, the onus should be on the creditor to satisfy the court that the debtor is guilty of the conduct alleged. Failure to satisfy the court that the debtor has been guilty of the alleged conduct should result in the debtor's immediate release.

(b) OVERVIEW OF THE PROPOSED PREJUDGMENT REMEDY

Having decided that, generally speaking, provisional relief should be available only against a debtor's property, we believe that it would be useful to outline briefly the Commission's proposals respecting this remedy. It is the view of the Commission that its proposed prejudgment remedy – which we shall call "attachment", although the remedy is not, strictly speaking, limited to seizure of a debtor's property – should be available only in limited circumstances, where there exist grounds that indicate a clear danger that a creditor's ultimate judgment will be rendered nugatory because of actions on the part of the debtor. The grounds for attachment are discussed below.

As to the method or methods of securing the debtor's property to which a court should be able to resort, we believe that flexibility should be the hallmark of this aspect of the proposed prejudgment remedy. Generally speaking, in order to ensure that a creditor's interests are adequately protected while, at the same time, minimizing the possible hardships that attachment might cause for debtors and others, a court would be authorized to order that a debtor's property be "attached" by any means, including physical or notional seizure (which the Commission has called "walking possession"[456]), registration of the attachment order under the

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[454] *Supra*, note 42.

[455] The Commission considers in some detail the possible impact of the *Canadian Charter of Rights and Freedoms* on the enforcement remedy of postjudgment arrest and imprisonment in Part V of its *Report on the Enforcement of Judgment Debts and Related Matters*: see ch. 3, sec. 8.

[456] See Commission Report, *supra*, note 1, Part II, ch. 2, at 113-19.

Personal Property Security Act,[457] enjoining the debtor from dealing with his property to the detriment of his creditors, or any combination of methods. These methods of attachment would take the place of the existing prejudgment remedies available against a debtor's property. Accordingly, we recommend that the *Absconding Debtors Act* and the absconding debtors provisions of the *Small Claims Courts Act* should be repealed. Finally, as we shall recommend that the courts, in ordering attachment, should be authorized expressly to grant a prejudgment injunction similar to a *Mareva* injunction,[458] we see no further need for the courts to continue to exercise the *Mareva* injunction jurisdiction that they now enjoy under section 19(1) of the *Judicature Act*.

The Commission has also considered whether the new attachment remedy should supersede section 22 of the *Family Law Reform Act*, dealing with prejudgment relief in the context of a support application.[459] Because the Act has been in force for only a short time, and because there do not appear to have been any problems under section 22, the Commission does not see any need to interfere with this remedy. Accordingly, we do not recommend the repeal of section 22 of the *Family Law Reform Act*. With the exception of this provision, however, the only authority for the courts to restrain debtors from dealing with their assets to the detriment of their creditors should be the new prejudgment attachment legislation that we propose herein.

The Commission believes that any new prejudgment relief legislation must also be hedged with safeguards to protect the rights of debtors and any third persons affected by such remedy. In this way, we would expect hardships to debtors and others to be minimized. We discuss below the nature and extent of the protections for debtors and others that should be enshrined in any new prejudgment relief legislation.[460]

(c) STATUTORY CONDITIONS FOR ATTACHMENT OF THE DEBTOR'S PROPERTY

We turn now to consider what a creditor should be required to show before the proposed prejudgment remedy of attachment should be granted.

(i) The Grounds for Attachment

Undoubtedly, the most important question with respect to provisional relief is the circumstances in which it should be available. As discussed previously, the existing provisions governing the grounds for attachment under Ontario's absconding debtors legislation are seriously deficient. The issue must be considered in light of the purpose of provisional relief, which is to provide a creditor with security to ensure that a future judgment against the debtor will result in more than simply a hollow victory.

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[457] R.S.O. 1980, c. 375.

[458] See *infra*, sec. 7(h).

[459] It is unnecessary to consider section 9 of the Act, as it deals with the preservation of property that is the subject matter of an action (see *supra*, sec. 3(c)) and therefore would be unaffected by our recommendations.

[460] See *infra*, sec. 7(i).

The Commission has given consideration to two basic approaches to this jurisdictional question. The first alternative would be to give to the courts a broad discretion to grant provisional relief whenever necessary to achieve the security objective of prejudgment attachment. The second alternative would be to specify in the proposed legislation the circumstances in which prejudgment attachment should be obtainable. The latter approach is the one that has found most favour in Canada and the United States.

Among the jurisdictions whose prejudgment attachment legislation we have examined, Quebec has elected to follow the first course. Article 733 of the Quebec *Code of Civil Procedure*[461] reads as follows:

> 733. The plaintiff may, with the authorization of a judge, seize before judgment the property of the defendant, when there is reason to fear that without this remedy the recovery of his debt may be put in jeopardy.

Although the Quebec approach to prejudgment attachment certainly has the advantage of flexibility, in the view of the Commission, the courts should be provided with guidelines concerning the circumstances in which prejudgment relief is appropriate. Given the nature of provisional relief, we believe that the legislature, and not the courts, should set the conditions for attachment. Accordingly, we reject the sort of legislation now in force in Quebec, which fails to specify the grounds for attachment and gives the courts an almost unfettered discretion to determine when attachment should be granted. Rather, we propose that Ontario's attachment legislation enumerate expressly the circumstances in which prejudgment attachment should be available. We turn then to consider those circumstances where attachment may be justified.

a. Departing from the Jurisdiction

Under Ontario's existing absconding debtors legislation, a person who is about to leave the jurisdiction intending to defraud his creditors, to avoid arrest, or to avoid being served with process is immune from prejudgment attachment. Only a person who actually has left the jurisdiction with the requisite intent is liable to have his property attached before judgment.[462] As we have pointed out, such a debtor is not likely to leave behind any exigible property.

In contrast to the provisions of the *Absconding Debtors Act* and the

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[461] R.S.Q. 1977, c. C-25.

[462] See the *Absconding Debtors Act*, *supra*, note 44, s. 3(1), and the *Small Claims Courts Act*, *supra*, note 45, s. 159(*a*). While section 159(*a*) would seem to permit attachment where the debtor is still in the jurisdiction, the affidavit prescribed by regulation speaks in terms of the debtor having departed: see discussion *supra*, sec. 2(b)(i)b.

Small Claims Courts Act, Rule 49.01(1)(c) of the Nova Scotia Rules provides that an attachment order may be secured where a debtor "is about to leave or has left the jurisdiction with intent to change his domicile, defraud his creditors, or avoid service of a document".[463] Both the Alberta Rules of Court[464] and the Saskatchewan *Absconding Debtors Act*[465] also allow for prejudgment attachment where the debtor "is about to abscond".

While the Commission agrees that prejudgment attachment should be possible where the debtor is about to depart from the jurisdiction with intent to defraud his creditors or to avoid being served with civil process, we do not favour resort to the attachment remedy on the grounds that the debtor is about to depart or has departed with intent to change his domicile or to avoid arrest. The Commission supports attachment in the first two intances because we believe that such conduct on the part of a debtor, by definition, reduces the likelihood that his creditor's collection efforts will be ultimately successful. As a result, the balance of interests in such circumstances is tipped in the creditor's favour.

Departing to change one's domicile, on the other hand, is a much more equivocal act on the part of the debtor. There may be any number of reasons why a person may wish to change his domicile that have nothing whatsoever to do with the claims of his creditors. And the same is true in the case of a debtor departing from the jurisdiction to avoid arrest. A debtor's flight from justice may be totally unrelated to the collection efforts of his creditors. If the Commission's recommendation for the abolition of prejudgment arrest of non-maintenance debtors is enacted,[466] arrest of such debtors will only be possible in criminal and quasi-criminal proceedings. A person fleeing arrest may well leave some or all of his property behind, and since he also may remain subject to the civil jurisdiction of the Ontario courts, his creditors may not be prejudiced by the debtor's departure or imminent departure.

Accordingly, the Commission recommends that prejudgment attachment should be available whenever a person is about to leave or has left Ontario with intent to defeat, defraud, hinder, or delay his creditors or any of them, or to avoid being served with civil process. We do not propose that a person should be liable to have his property attached before judgment on the ground that he is about to leave or has left the jurisdiction with intent to avoid arrest or to change his domicile. Provisional relief in the form of attachment in these latter instances would not be consonant with the policy behind such relief, namely, providing a creditor with security for a future judgment where enforcement of the judgment may be frustrated by the actions of his debtor.

b. Concealment

Closely related to departing from the jurisdiction to avoid service of civil process as a ground for attachment is the debtor's keeping himself concealed to avoid service of civil process. Concealment is now a ground for attachment under the *Small Claims Courts Act*,[467] but not under the *Absconding Debtors Act*. The provision in the New York Civil Practice Law and Rules is somewhat broader in scope, since it authorizes attachment where the debtor "resides or is domiciled in the state and cannot be personally served despite diligent efforts to do so".[468]

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[463] See , also, r. 49.01(1)(c) of the Prince Edward Island Rules.

[464] *Supra*, note 89, r. 485(a)(i).

[465] R.S.S. 1978, c. A-2, s. 3(1)(*a*).

[466] See *supra*, sec. 7(a).

In the view of the Commission, a debtor who conceals himself to avoid service of civil process should be treated no differently than one who leaves the jurisdiction with the same goal in mind. The debtor's motive and the probable consequences to his creditor are the same in each instance. The fact that a debtor who conceals himself may remain in the jurisdiction is irrelevant. The debtor's actions in each case are a reasonable indication that the debtor is likely to take steps to frustrate the enforcement activities of his creditor.

We wish to make clear that we are not suggesting that, where the debtor has concealed himself to avoid service, prejudgment attachment should be used to give an Ontario court jurisdiction *in personam* over the creditor's claim. Indeed, as will be discussed below, we reject the use of attachment as a jurisdictional device.[469] In other words, we believe that, in order for an Ontario court to assume jurisdiction over the debtor, the creditor should still have to serve the debtor with originating process in accordance with the rules of procedure, or the debtor should have to submit or consent to the court's jurisdiction. However, we do not deny that the attachment of his property may well operate as an incentive to the debtor to make himself amenable to service of civil process.

Accordingly, the Commission recommends that concealment by the debtor to avoid service of civil process should be a ground for prejudgment attachment of the debtor's property.

c. The Debtor Dealing with his Property

One of the most obvious weaknesses of the Ontario *Absconding Debtors Act* is its failure to allow a creditor to obtain an order of attachment against his debtor where the latter has dealt with, or is dealing with, his property in a way that is clearly detrimental to the creditor, for example, by removing his property from the jurisdiction or by concealing it. While section 159(*b*) of the *Small Claims Courts Act* provides for prejudgment attachment where the debtor "attempts to remove . . . property out of Ontario or from one county to another therein with intent to defraud", this provision would not help a creditor whose debtor has dealt with his property in some other way that indicates *mala fides* on his part.

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[467] *Supra*, note 45, s. 159(*c*). Such a provision can be found in the attachment legislation of most Canadian provinces: see, for example, Alberta Rules of Court, *supra*, note 89, r. 485(a)(iii); Manitoba Queen's Bench Rules, *supra*, note 89, r. 582(a); *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2, s. 2; Nova Scotia Rules, r. 49.01(1)(b); Prince Edward Island Rules, r. 49.01(1)(b); and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 3(1)(*c*).

[468] N.Y. Civ. Prac. Law §6201.2 (McKinney).

[469] See discussion *infra*, sec. 7(d).

In the absconding debtors legislation of other Canadian jurisdictions, provision has been made for a right of attachment before judgment where the debtor deals with his property with a view to impeding the future enforcement efforts of his creditors. For example, the Saskatchewan *Absconding Debtors Act*[470] permits attachment where the debtor "has attempted to remove [non-exempt] personal property out of Saskatchewan or to sell or dispose of it with intent to defraud his creditors generally or the plaintiff in particular". The Manitoba Queen's Bench Rules authorize the making of an attachment order where the debtor "is about to remove or transfer any of his personal property from Manitoba, or has assigned, transferred, disposed of, or secreted, or is about to assign, transfer, dispose of, or secrete any of his property with intent to delay, defeat, or defraud his creditors".[471]

The Nova Scotia Rules and the Prince Edward Island Rules contain somewhat broader provisions. An attachment order may be secured in each case if the debtor "is about to remove or has removed his property or any part thereof permanently out of the jurisdiction"[472] or "has concealed, removed, assigned, transferred, conveyed, converted or otherwise disposed of all or any of his property with intent to hinder or delay his creditors, or is about to do so".[473] Although the California Code of Civil Procedure contains no similar provision, a creditor may resort to the *ex parte* attachment procedure where he can show "that great or irreparable injury would result . . . if issuance of the order were delayed until the matter could be heard on notice".[474] This requirement may be satisfied by evidence that shows that "there is a danger that the property sought to be attached would be concealed, *substantially impaired in value, or otherwise made unavailable* to levy if issuance of the order were delayed until the matter could be heard on notice".[475]

It may be contended that conduct of the kind covered by the abovementioned Nova Scotia Rules and the Prince Edward Island Rules is the proper subject matter of voidable transactions legislation, such as that proposed in chapter 3. However, a number of arguments may be marshalled against this view. First, voidable transactions legislation is not broad enough to cover concealment or removal of property by the debtor. Secondly, even in the case of a conveyance of property by the debtor, such legislation in many cases will be an inadequate deterrent against questionable transactions. Prejudgment attachment, on the other hand, would enable a creditor to prevent the debtor from acting to prejudice his future enforcement activity. Thirdly, the cost of impeaching a voidable transaction generally will far exceed the minor costs involved in taking attachment proceedings, making the latter a more effective and economical enforcement remedy.

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[470] R.S.S. 1978, c. A-2, s. 3(1)(*b*).

[471] *Supra*, note 89, r. 582(c).

[472] R. 49.01(1)(d).

[473] R. 49.01(1)(e).

[474] West's Cal. Code Civ. Pro. (1982), §485.010(a).

[475] *Ibid.*, §485.010(b)(1) (emphasis added). Such a showing also entitles a creditor to a temporary protective order: see §486.010(b).

Accordingly, the Commission is of the belief that this most serious gap in Ontario's attachment legislation must be remedied. Moreover, we are of the view that the ambit of the legislation in this respect should be sufficiently broad to encompass a wide variety of actions intended by a debtor to frustrate the collection efforts of his creditor. Therefore, the Commission recommends that a debtor who has removed his property from the Province, or is about to remove his property from the Province, or who has assigned, transferred, disposed of, encumbered or secreted his property, or is about to assign, transfer, dispose of, encumber or secrete his property, with intent to defeat, defraud, hinder, or delay any of his creditors, or who has done or omitted to do any act with respect to his property with intent to frustrate the enforcement of a judgment that might be obtained by the creditor, should be liable to have his property attached before judgment.

d. Fraudulent Incurring of Liability by the Debtor

In some jurisdictions, the nature of the creditor's claim itself is sufficient to support an application for attachment; for example, an attachment order may be obtained under Rule 49.01(1)(f) of the Nova Scotia Rules if the debtor "has fraudulently incurred a debt or liability in issue in a proceeding".[476] Whether the debt or liability sounds in contract or in tort would seem to be irrelevant under this provision.

The principal justification for permitting a creditor to attach the property of his debtor before judgment simply because the debtor's liability was incurred fraudulently would seem to be an assumption that such a debtor is more likely than not to take steps to impede his creditor's efforts to make good his loss.

In our view, the nexus between the particular nature of the creditor's claim and his need for security seems considerably more tenuous than is the case with the grounds of attachment recommended above. Moreover, we question the validity of the supposition upon which attachment in such circumstances would seem to be based. Permitting attachment on this basis assumes that the debtor is indeed guilty of the alleged fraud. Were attachment allowed in these circumstances, the risk to the debtor would be magnified: injury to his personal or business reputation might well be greater than if attachment were granted on other grounds. Moreover, even if the abovestated assumption were valid, the risk to creditors would seem to be increased only marginally by requiring them to establish one of the other proposed grounds for attachment. Consequently, we recommend that prejudgment attachment should not be available on the ground that the debt or liability of the debtor is alleged to have been incurred fraudulently.

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[476] See also r. 49.01(1)(f) of the Prince Edward Island Rules.

e. Nonresidence of the Debtor

In many jurisdictions, a debtor's property may be attached before judgment on the ground that he is a nonresident. This is the case in Nova Scotia[477] and in Prince Edward Island,[478] and to a more limited extent in Manitoba.[479] The same is true in all three of the American jurisdictions whose attachment legislation we examined earlier in this chapter.[480] Indeed, the nonresidence of the debtor is now the only ground for prejudgment attachment in Michigan.[481]

The assumption underlying this ground of attachment would seem to be that a nonresident debtor presents a greater danger to his creditor than a resident debtor. Once again, we question the correctness of this assumption.

In our view, there is no necessary relationship between the debtor's nonresidence and the need of his creditors for security for a future judgment. Moreover, at the time the debt was contracted, the creditor may have known that the debtor was a nonresident, and may have accepted the risk of dealing with a nonresident. Therefore, we recommend that the mere fact that the debtor is a nonresident of Ontario should not be sufficient to support prejudgment attachment of the debtor's property.

f. The Need for a "Basket Clause"

At an earlier juncture, we indicated that we favoured the adoption of a legislative scheme that would delineate the circumstances in which prejudgment attachment should be obtainable.[482] The Commission has also considered whether the interests of creditors would be better safeguarded by the inclusion of a "catch-all" provision that would enable a court to order attachment where, for example, there is a danger that failure to grant provisional relief would jeopardize recovery of a debt.

It may be argued that such a "basket clause" would be inconsistent with the general approach to the grounds for attachment adopted by the Commission, and that a court, relying on such a provision, might grant prejudgment relief in inappropriate cases. However, on balance, we have concluded that the proposed legislation governing attachment should contain a basket provision. First, we are concerned that no list of criteria can purport to be exhaustive; a basket provision would give the court flexibility to do justice in the circumstances of the individual case. Secondly, we shall be subsuming, under the proposed attachment remedy,

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[477] Nova Scotia Rules, r. 49.01(1)(a).

[478] Prince Edward Island Rules, r. 49.01(1)(a).

[479] Manitoba Queen's Bench Rules, *supra*, note 89, r. 582(b).

[480] See West's Cal. Code Civ. Pro. (1982), §§492.010-492.090; N.Y. Civ. Prac. Law §6201.1 (McKinney); and Mich. C.L.A., §600.4001.

[481] The Michigan Law Revision Commission has recommended that even this ground for attachment should be abolished: see discussion *supra*, sec. 6(b)(ii)b.

[482] See *supra*, sec. 7(c)(i).

Mareva injunctions, which are now available under section 19(1) of the *Judicature Act*.[483] Section 19(1) gives the court broad jurisdiction to grant relief "in all cases in which it appears to the court to be just or convenient" to do so. In light of the caution and restraint exercised by the courts under section 19(1), we are confident that the courts would employ a basket provision only in appropriate circumstances. Moreover, we are of the view that our recommendations concerning the specific instances in which prejudgment relief should and should not be available will provide courts with considerable guidance in respect of the manner in which the discretion inherent in a "basket clause" should be exercised. Accordingly, we recommend that, in addition to the specific grounds for attachment proposed above, courts should be empowered to grant prejudgment relief whenever there is a danger that, without such relief, recovery of a debt may be jeopardized.

(ii) Subsidiary Issues

a. The Debtor's Residence

Ontario's *Absconding Debtors Act*,[484] though not the absconding debtors provisions of the *Small Claims Courts Act*,[485] makes residence in Ontario on the part of the debtor a precondition to attachment. The attachment rules recently enacted in Nova Scotia[486] and Prince Edward Island[487] contain no similar requirement; indeed, specific provision is made for attachment where the debtor "resides out of the jurisdiction, or is a corporation that is not registered . . .".[488] In this respect, the Nova Scotia Rules and the Prince Edward Island Rules resemble the attachment laws in many American jurisdictions.

The Commission is of the opinion that a residency requirement is anachronistic. Restricting the availability of prejudgment attachment to resident debtors may have made sense when the courts of Ontario had only limited jurisdiction over nonresident defendants. But this certainly is no longer the case. Indeed, it seems somewhat inconsistent to limit attachment to resident debtors when the Supreme Court of Ontario Rules of Practice[489] allow Ontario courts to assume jurisdiction over many nonresident debtors by virtue of the rules governing service *ex juris* of originating process. We can see no reason to prohibit the attachment of property in Ontario in the case of a nonresident debtor; to do so would mean that the access to Ontario courts provided by the Rules of Practice would be little more than illusory in many cases. Therefore, we recommend that attachment should be available under Ontario law whether or not the debtor is an Ontario resident.

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[483] See *infra*, sec. 7(h).

[484] *Supra*, note 44, s. 2(1).

[485] *Supra*, note 45, ss. 159-73.

[486] Nova Scotia Rules, r. 49.

[487] Prince Edward Island Rules, r. 49.

[488] Nova Scotia Rules, r. 49.01(1)(a), and Prince Edward Island Rules, r. 49.01(1)(a).

[489] *Supra*, note 15, r. 25.

b. Types of Claim

At the present time, prejudgment attachment is available in Ontario only if the creditor's claim against the debtor sounds in debt or damages arising out of a contract.[490] While similar restrictions can be found in the absconding debtors legislation of most provinces,[491] neither the Nova Scotia nor the Prince Edward Island attachment rules seek to limit the availability of prejudgment attachment in this way.

In the United States, the type of claim that will support an application for attachment varies from one jurisdiction to the next. For example, in California, attachment may be sought "only in an action on a claim or claims for money, each of which is based upon a contract, express or implied".[492] Under section 6201 of the New York Civil Practice Law and Rules, on the other hand, the nature of the creditor's underlying claim is irrelevant. As a result of some recent cases, it now would appear that a creditor is free to claim a *Mareva* injunction whether his action sounds in tort or contract and whether it is commercial or non-commercial in nature.[493]

For a variety of reasons, the Commission believes that prejudgment attachment should be obtainable no matter what sort of claim the creditor asserts against his debtor. First, in our opinion, to restrict this remedy to claims for "debt", "debt or liquidated demand", or "debt, demand or claim" would give rise to a substantial amount of unnecessary and unhelpful litigation; indeed, uncertainty about the meaning of terms such as "debt" and "debt or liquidated demand" has produced just such a result in other areas of the law.[494]

Secondly, we are of the view that, unless there are strong reasons to the contrary, the law should afford equal protection to creditors, and there does not seem to be any good reason to differentiate, for example, between a potential contract creditor and a tort creditor. Indeed, where the latter is seeking damages for injuries suffered as a direct result of the actions of the debtor, attachment may be even more important than in a commercial case; after all, a commercial creditor normally would be in a position to ask for some security from the debtor before entering into a transaction.

We are also unable to accept the argument that confining prejudgment attachment to cases of debt or contract is likely to reduce substantially the possibility of wrongful attachment. It is easy to envisage complex commercial litigation where the merits of the creditor's claim are far from straightforward. Not even all actions for debt are simple and uncomplicated.

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[490] See the *Absconding Debtors Act*, *supra*, note 44, s. 3(1), and the *Small Claims Courts Act*, *supra*, note 45, s. 159.

[491] See, for example, Alberta Rules of Court, *supra*, note 89, r. 485; *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2, s. 2; and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 3. Compare *The Judicature Act*, R.S.N. 1970, c. 187, s. 82(1)(c).

[492] West's Cal. Code Civ. Pro. (1982), §483.010.

[493] See discussion *supra*, sec. 3(a).

[494] See discussion *supra*, sec. 2(b)(ii)d.(2).

Consequently, we recommend that prejudgment attachment should be available to all creditors, irrespective of the nature of their underlying claim. The protection theoretically afforded debtors by the present restriction of this remedy to actions in debt or sounding in contract can be provided in other ways, such as the introduction of substantial procedural safeguards.[495]

c. *The Amount in Dispute*

Some jurisdictions have sought to limit possible creditor abuse of prejudgment attachment by providing that such relief is obtainable only where the creditor's claim exceeds a certain minimum amount. The $100 minimum found in the *Absconding Debtors Act*[496] and the $4 minimum set by the *Small Claims Courts Act*[497] probably have had little impact on the use of the remedy of attachment. These figures, of course, could be raised to account for the effects of inflation, and therefore better serve the theoretical basis for their original introduction into Ontario's absconding debtors legislation.

Other Canadian jurisdictions are divided on the matter of a minimum claim. Legislation in Nova Scotia,[498] Prince Edward Island,[499] and Quebec[500] providing for a right of prejudgment attachment contains no such minimum. In the other provinces, the minimum claim required to support an applicaton for prejudgment attachment varies from a low of $20[501] to a high of $200.[502]

A similar division can be seen in the prejudgment attachment provisions of the American jurisdictions that we have examined. For example, in New York prejudgment attachment is available regardless of the amount in dispute. California, on the other hand, recently has increased its minimum from $200 to $500,[503] and the California Law Revision Commission supported the use of such a screening device.[504] The Commission was of the view that a $500 minimum claim requirement "tends to eliminate those cases where consumer necessities might be attached".[505] It noted that this figure corresponded to the jurisdictional limit of the state's small claims court. The California Law Revision Commission believed that, since a creditor seeking to collect a lesser amount would have available to him an expeditious procedure, he would have less need for prejudgment attachment. Another reason for the Commission's support of a minimum claim requirement was the husbanding of judicial resources. The Commission stated that "the elimination of these relatively small cases helps to save court time and resources which are inefficiently employed to collect small debts under the attachment procedure".[506]

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[495] See *infra*, sec. 7(i).

[496] *Supra*, note 44, s. 3(1).

[497] *Supra*, note 45, s. 159.

[498] Nova Scotia Rules, r. 49.

[499] Prince Edward Island Rules, r. 49.

[500] *Code of Civil Procedure*, R.S.Q. 1977, c. C-25, arts. 733-40.

[501] *The Judicature Act*, R.S.N. 1970, c. 187, s. 82.

[502] Alberta Rules of Court, *supra*, note 89, r. 485.

[503] See now West's Cal. Code Civ. Pro. (1982), §483.010.

[504] California Law Revision Commission, *supra*, note 385, at 723-24.

[505] *Ibid.*, at 723.

We do not find the reasons given by the California Law Revision Commission persuasive. First, in our view, protection for necessities can be provided in a much more direct and effective manner, without prejudicing the right of creditors to look to non-necessities.

Secondly, the existence of an expeditious legal procedure for the determination of legal disputes does not obviate the need for provisional relief. Indeed, as we have mentioned, the *Small Claims Courts Act* itself provides for the prejudgment attachment of an absconding debtor's property. Moreover, it is interesting to note that the English courts have refused to restrict the availability of *Mareva* injunctions to cases other than those in which a summary judgment procedure may be used.[507] We are in agreement with this flexible approach to prejudgment relief.

Finally, we find the judicial economy argument put forth by the California Law Revision Commission less than compelling. We cannot, of course, ignore the realities of existing and future constraints on judicial resources. However, judicial economy is but one factor among many that should be considered in deciding whether prejudgment attachment should be available to creditors with small claims. Moreover, judicial economy arguments can be used to support provisional relief in the circumstances under consideration here. Is there not also a squandering of limited judicial resources if a creditor is unable to enforce his judgment because his debtor has been allowed to dispose of his assets in the interim?

Accordingly, the Commission recommends that prejudgment attachment should be available regardless of the amount claimed by a creditor in his main action.

(d) PREJUDGMENT ATTACHMENT AND MATTERS OF JURISDICTION

Having discussed the factual grounds for prejudgment attachment of a debtor's property, we turn to consider two closely related matters, namely, whether attachment should be available to a creditor where the Ontario courts would be unable to assume jurisdiction over the main dispute, and whether attachment of a debtor's property should be sufficient, in and of itself, to found such jurisdiction. To some extent, these questions are really two sides of the same coin. However, we are of the view that they should be dealt with separately.

Generally speaking, the jurisdiction of a court in Ontario to hear any dispute depends upon the court being able to assume personal jurisdiction over the defendant in the action. Jurisdiction *in personam* can be acquired at common law only by service of originating process on the defendant or by the defendant's submission or consent to such jurisdiction. Pursuant to the Supreme Court of Ontario Rules of Practice,[508] service of originating process can be effected either within or without Ontario. However, service *ex juris* is possible only in those circumstances outlined in Rule 25 of the Ontario Rules of Practice, and even with the recent liberalization of this Rule,[509] there still may be occasions when service *ex juris* will not be possible.

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[506] *Ibid.*

[507] See *Rasu Maritima SA v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara (Pertamina)*, *supra*, note 251, at 333-34, *per* Lord Denning M.R.

It may be argued that, where an Ontario court does not have jurisdiction *in personam* over the main action, prejudgment attachment of the debtor's property in Ontario is inappropriate. After all, what need can there be for security if there can be no future Ontario judgment? On the other hand, it may be contended that the possibility of a judgment from an Ontario court at some time in the future cannot be foreclosed entirely. For example, a foreign debtor may come to Ontario, and he then may be served with originating process. Moreover, there is always the possibility of the creditor securing a judgment against the debtor in a foreign jurisdiction, and the judgment may well be one that would be recognized by the Ontario courts,[510] and therefore capable of being enforced here. In such a case, attachment of the debtor's property in Ontario certainly would help to secure the creditor's judgment, albeit a foreign judgment.

This very issue came before the House of Lords in *Siskina (Cargo Owners) v. Distos Compania Naviera SA*,[511] a case concerned with the availability of a *Mareva* injunction. While a majority of the English Court of Appeal had held that a *Mareva* injunction was available irrespective of the jurisdiction of the English courts to determine the main dispute, the law lords unanimously concluded that such relief could be claimed only if the main action was justiciable in England.

We are in agreement with the conclusion of the House of Lords in *Siskina (Cargo Owners) v. Distos Compania Naviera SA*. While this conclusion was based in large part on the wording of the English equivalent of Rule 25 of the Ontario Rules of Practice,[512] we believe that it can be supported on grounds of public policy. As we have stated earlier, a just and equitable law of prejudgment attachment requires that the interests of debtors and creditors be balanced evenly. Attachment of a person's property on the contingency that, at some future time, the Ontario courts will have jurisdiction over that person poses serious risks to the debtor, risks that we believe outweigh the posssible benefit to his creditor.

To avoid such a conclusion, we believe it would be necessary to decide that prejudgment attachment should be sufficient to give an Ontario court jurisdiction over the main dispute, even though the court otherwise could not assume jurisdiction. As we have seen, attachment as a jurisdictional device, or foreign attachment, is a common feature of attachment legislation in the United States. However, for constitutional reasons, this *quasi in rem* jurisdiction has come under increasing attack from the courts in recent years.[513]

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[508] *Supra*, note 15, r. 25.

[509] O. Reg. 106/75, s. 26(4).

[510] For a discussion of the law concerning the recognition of foreign judgments, see Castel, *Canadian Conflict of Laws* (1975), ch. 14.

[511] [1979] A.C. 210, [1977] 3 W.L.R. 818, [1977] 3 All E.R. 803 (H.L.) (subsequent references are to [1977] 3 All E.R.).

[512] Rules of the Supreme Court 1965, Ord. 11, r. 1.

The House of Lords in *Siskina (Cargo Owners) v. Compania Naviera Distos SA* also considered the argument that an English court should have jurisdiction over an action on the ground that, in the circumstances of the case, a *Mareva* injunction was justified. This contention was rejected by the House of Lords, Lord Diplock commenting as follows:[514]

> To argue that the claim to monetary compensation is justiciable in the High Court because if it were justiciable it would give rise to an ancillary right to a Mareva injunction restraining the shipowners doing something in England pending adjudication of the monetary claim, appears to me to involve the fallacy of petitio principii or, in the vernacular, an attempt to pull oneself up by one's own bootstraps.

For all the above reasons, the Commission recommends that prejudgment attachment should be available only in those cases where the Ontario courts would have jurisdiction *in personam* over the defendant, pursuant to the principles at common law or under Rule 25 of the Supreme Court of Ontario Rules of Practice.

(e) Timing of the Creditor's Application for Prejudgment Relief

We now turn to consider whether prejudgment relief should be available both before and after a creditor has launched his suit against the debtor.

Under section 2(2) of the Ontario *Absconding Debtors Act*, a creditor may apply for an order of attachment "only in a pending action". A warrant of attachment may be secured in the small claims courts, on the other hand, at or following the commencement of an action.[515] Other Canadian absconding debtors and attachment legislation generally prohibits the prejudgment attachment of a debtor's property before the institution of legal proceedings to resolve the main dispute between the debtor and his creditor.[516]

However, there are some jurisdictions where a creditor is able to attach a debtor's property even before he has initiated legal proceedings against the debtor. This is the case, for example, under the New York attachment legislation.[517] However, an order of attachment issued prior to the commencement of the creditor's suit remains valid "only if, within sixty days after the order is granted, a summons is served upon the defendant".[518]

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[513] See, for example, *Shaffer v. Heitner*, *supra*, note 403, and *Rush v. Savchuk*, *supra*, note 404.

[514] *Supra*, note 511, at 825 (emphasis deleted).

[515] *Small Claims Courts Act*, *supra*, note 45, ss. 162 and 163.

[516] See, for example, Alberta Rules of Court, *supra*, note 89, r. 485; Manitoba Queen's Bench Rules, *supra*, note 89, r. 582; and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 3(1).

From the debtor's perspective, prejudgment attachment prior to the commencement of an action may increase the dangers that are inherent in provisional relief. It may be argued that the law should not lend its support to efforts to deprive the debtor of his property where his creditor has failed to show his *bona fides* by the institution of legal proceedings; after all, the creditor need only issue a writ of summons.

On the other hand, it may be contended that there may well be instances when the purpose of prejudgment attachment – providing the creditor with interim security – would be defeated by a requirement that legal proceedings be instituted before an application for attachment can be heard. Granted, the institution of legal proceedings may be a mere formality under the present rules of civil procedure, one with which a creditor can easily comply.[519] However, it is certainly possible to envisage a case where the creditor learns of the questionable actions of his creditor at a time when the offices of the courts are closed, and originating process cannot be issued; in such circumstances, any delay in attaching the debtor's property may be fatal to the creditor's chances of ultimate recovery. As long as the risk to the debtor can be minimized, the Commission sees no convincing reason why the law should prohibit prejudgment attachment until the creditor has complied with the formality of instituting a suit against the debtor.

We are fortified in our view by the proposals of the Payne Committee in this regard. It will be recalled that the Payne Committee Report anticipated the development of the *Mareva* injunction. The Report proposed that a court should be authorized to grant injunctive relief, like that now available in England by means of a *Mareva* injunction, even before an action has been commenced, but should do so upon terms that originating process is issued "on the next day on which the court office is open".[520]

While we agree with the thrust of this recommendation, we believe that it may not be sufficiently flexible. The Commission is of the opinion that the interests of debtors and creditors would be best protected by allowing attachment to issue prior to the commencement of an action upon such terms and conditions respecting the commencement of an action as seem just. Such a power would be similar to the discretion that the Ontario courts now exercise in granting prejudgment injunctive relief generally.[521]

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[517] N.Y. Civ. Prac. Law §6213 (McKinney).

[518] *Ibid.*

[519] Rules of Practice, *supra*, note 15, rr. 5 and 32. Under the rules proposed by the Civil Procedure Revision Committee, an action, generally speaking, would be commenced by the issuance of a Statement of Claim: see Williston Committee Rules, *supra*, note 26, r. 16.03(1). However, the proposed rules would also allow an action to be initiated by a Notice of Action, "[w]here there is insufficient time to prepare a Statement of Claim": see r. 16.03(2). A Notice of Action is similar in form and detail to a writ of summons.

[520] Payne Committee Report, *supra*, note 238, para. 1254, at 324.

Accordingly, the Commission recommends that prejudgment attachment should be available irrespective of whether the creditor has commenced an action against the debtor, and that attachment before litigation has been initiated should be available upon such terms and conditions respecting the commencement of the action as to the court seem just.

(f) PROPERTY SUBJECT TO PREJUDGMENT ATTACHMENT

In earlier Parts of the *Report on the Enforcement of Judgment Debts and Related Matters*, we considered what kinds of property should be subject to the enforcement remedies of seizure and sale[522] and garnishment.[523] We now must answer the same question in the context of provisional relief.

It may be useful to begin this discussion by pointing out the present legislative response to this question. Under Ontario's *Absconding Debtors Act*, attachment may be used to reach a debtor's exigible real property and personal property,[524] including debts owed to him by third persons.[525] In contrast, only a debtor's exigible personal estate and effects may be taken under a writ of attachment issued by a small claims court.[526]

We see no reason to depart from our earlier recommendations on this subject, nor indeed from the thrust of Ontario's present *Absconding Debtors Act*. Therefore, subject to the exemptions proposed below, we recommend that all the debtor's property, real and personal, debts included, should be subject to prejudgment attachment.

It should be noted that this recommendation would permit the attachment of debts owed to a small claims court debtor by a third person, something that has not been possible since the abolition of prejudgment garnishment in the small claims courts in 1977. In our view, the safeguards that we propose below, as well as the fact that we recommend in the next section that wages, salary, and other similar income should be exempt from prejudgment attachment, would minimize the dangers in such a case.

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[521] See s. 19(1) of the *Judicature Act*, *supra*, note 27, which provides as follows:

> 19.-(1) A mandamus or an injunction may be granted . . . in all cases in which it appears to the court to be just or convenient that the order should be made, and any such order may be made either unconditionally or upon such terms and conditions as the court considers just . . . .

Interlocutory injunctions have been granted before the institution of legal proceedings: see, for example, *Thorneloe v. Skoines* (1873), L.R. 16 Eq. 126.

[522] See Commission Report, *supra*, note 1, Part II, ch. 2, and Part III.

[523] *Ibid.*, Part II, ch. 3.

[524] *Supra*, note 44, s. 7.

[525] *Ibid.*, ss. 14-16.

[526] *Small Claims Courts Act*, *supra*, note 45, s. 159.

While provisional relief, by definition, entails some risk to debtors, in the Commission's view the degree of risk would be virtually unaffected by the nature of the property taken as security. Of much greater importance is the method of attachment employed, a subject that is explored below.[527]

(g) PROPERTY EXEMPT FROM PREJUDGMENT ATTACHMENT

Regarding the nature of exemptions from the prejudgment remedy of attachment, two separate issues must be addressed. First, should the exemptions recommended earlier in the context of postjudgment enforcement activity apply as well to prejudgment attachment? Secondly, given the nature of provisional relief, should a debtor be able to claim additional exemptions?

Insofar as the applicability of the proposed postjudgment exemptions to prejudgment relief is concerned, it may be contended, on the one hand, that none of these exemptions should be available: the debtor by his conduct may be said to have disentitled himself to the protection of the law. Moreover, in the circumstances contemplated, to prefer the interests of the creditor over those of his debtor would not seem to be inequitable. On the other hand, it may be argued that to disentitle a debtor to the proposed exemptions would be a self-defeating exercise. Depriving a debtor of these exemptions may result in the debtor and his family being thrown on the public purse, or may render the debtor simply less capable of ultimately satisfying any judgment the creditor obtains against him. Finally, and perhaps most importantly, given the fact that no final adjudication of the merits of the creditor's claim will have taken place, to strip the debtor of the proposed exemptions on attachment may be to tip the scales of justice unduly in the creditor's favour.

Legislation in most Canadian jurisdictions today provides that only the property of the debtor liable to seizure under execution may be attached;[528] in other words, the postjudgment exemptions may be claimed by a debtor subject to prejudgment attachment. This is certainly the case under both the Ontario *Absconding Debtors Act*[529] and the *Small Claims Courts Act*.[530]

It should be noted, however, that the Commission, in Part II of the *Report on the Enforcement of Judgment Debts and Related Matters*, recommended that certain debtors should be deprived in whole or in part of the exemptions generally available in the postjudgment context. In chapters 2 and 3 of Part II, for example, we proposed that a maintenance debtor should be entitled to substantially reduced exemptions.[531] We are of the view that the policy considerations underlying this exception apply equally to prejudgment enforcement efforts. In short, the needs of the maintenance debtor must be balanced against the needs of the maintenance creditor.

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[527] See *infra*, sec. 7(h).

[528] See, for example, Manitoba Queen's Bench Rules, *supra*, note 89, r. 590; *Absconding Debtors Act*, R.S.N.B. 1973, c. A-2, s. 13; Nova Scotia Rules, r. 49.04(1)(a); and Prince Edward Island Rules, r. 49.04(1)(a).

[529] *Supra*, note 44, s. 7: "All the property of an absconding debtor liable to seizure under execution may be attached . . .".

[530] *Supra*, note 45, s. 159.

In chapters 2 and 3 of Part II of the *Report on the Enforcement of Judgment Debts and Related Matters*, we also proposed that a debtor who is about to abscond or has absconded from the jurisdiction with the intent to defeat, defraud, hinder, or delay any of his creditors should not be allowed to claim any exemptions.[532] This recommendation was based on the belief that a debtor who intends to renounce or who actually renounces his legal obligations under provincial law by absconding disentitles himself to the benefits of legislation enacted for the protection of debtors. However, given the nature of prejudgment attachment, we are not convinced that the abovementioned rationale for depriving absconding debtors of their exemptions applies with equal force in the prejudgment context. In the absence of a judgment against the debtor, we believe that he should be given the benefit of any doubt.

Consequently, we recommend that all debtors subject to prejudgment attachment should be able to claim those exemptions proposed by the Commission in the postjudgment context, irrespective of the grounds for attachment. In the case of a maintenance debtor, this will mean that he or she will be entitled to reduced exemptions; an absconding debtor will be entitled to claim the postjudgment exemptions to which he would be entitled if he were not an absconding debtor.

Turning to the second issue, apart from wages, salary, and other similar income, discussed below, we do not support the contention that a debtor subject to prejudgment attachment warrants additional exemptions. It will be recalled that, in California, in addition to the ordinary exemptions, section 487.020 of the Code of Civil Procedure now provides that all "[p]roperty which is necessary for the support of an individual defendant or the defendant's family supported in whole or in part by the defendant" is exempt from attachment.

For the following reasons, we do not believe that such a "necessities exemption" should be included in the proposed attachment legislation. First, we are of the view that, in many cases, the prejudgment remedy of attachment would be rendered useless by such a broad exemption. Secondly, given the limited grounds for prejudgment attachment that we have proposed, such an exemption seems unduly charitable. Thirdly, there is the matter of the uncertainty that would result from the inclusion of an exemption similar to section 487.020 of the California Code of Civil Procedure. Finally, the Commission is of the view that the procedural safeguards that are proposed below[533] will go a long way towards ensuring that debtors are not driven to the wall by prejudgment attachment.

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[531] Commission Report, *supra*, note 1, Part II, ch. 2, at 90-96, and ch. 3, at 171-74.

[532] *Ibid.*, ch. 2, at 99, and ch. 3, at 175-76.

However, we do believe that wages, salary, and other similar income deserve a special status. The present prohibition[534] against the prejudgment garnishment and attachment of such income in most Canadian jurisdictions can be seen as a recognition of the uniqueness of this particular asset. Similarly, the United States Supreme Court, in *Sniadach v. Family Finance Corp. of Bay View*,[535] in concluding that the prejudgment garnishment of an individual's wages without prior notice or an opportunity to be heard was unconstitutional, placed special emphasis on the nature and importance of wages to the individual debtor and his family. It is the opinion of the Commission that, since the vast majority of the public survive day-to-day on their employment income, to allow any such income to be attached before judgment would be too burdensome to the average debtor and his family.

Accordingly, the Commission recommends that a debtor's wages, salary, and other similar income should be exempt entirely from prejudgment attachment, and that the normal *prima facie* eighty-five percent exemption proposed by the Commission in Part II of this Report should not apply.[536]

(h) THE METHOD OF ATTACHMENT

Having dealt with the property of a debtor that should be subject to prejudgment attachment, we turn to a discussion of the method or methods of attachment that should be available. In considering this matter, we have been motivated by one concern: given the security function of prejudgment attachment, how can a debtor's property be "taken" as security, while at the same time minimizing the risk to the debtor.

The method of attachment will have important consequences for debtors, particularly where physical seizure is employed. One of the major criticisms of prejudgment attachment in the United States has been the harm that a debtor whose property is seized under attachment may suffer as a result of being deprived of the use of the property until judgment.[537] Of course, the degree of harm may vary with the type of debtor and the type of property; however, both individual debtors and business debtors may be prejudiced by prejudgment attachment. Indeed, the corporate debtor may be at greater risk, for, unlike the individual debtor, it will have no statutory exemptions. This is to say nothing of the indirect effects of provisional relief, such as damage to the debtor's credit rating, his reputation and, in some cases, bankruptcy.

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[533] See *infra*, sec. 7(i).

[534] See the discussion respecting prejudgment garnishment, *supra*, sec. 2(b)(ii), where many of the legislative provisions are described.

[535] *Supra*, note 372, discussed *supra*, sec. 6(b)(i).

[536] See Commission Report, *supra*, note 1, Part II, ch. 3, at 168.

[537] See, for example, Zaretsky, "Attachment Without Seizure: A Proposal for a New Creditors' Remedy", [1978] U. Ill. L.F. 819.

Commentators also have pointed to the societal costs of prejudgment attachment that result from the debtor being deprived of his property. Zaretsky has commented as follows on this subject:[538]

> Attachment of a business debtor's property provides even greater potential for economic waste. If his equipment is attached, his productive capacity is reduced or idled, and society loses the benefit of that production.

Where prejudgment attachment proceedings involve third parties, such as a co-owner of property or the person from whose possession the property attached is taken, they too will incur certain expenses.[539] Societal costs may arise in other ways as well. For example, the extent to which provisional relief may be used as a threat or lever to force a settlement may be said to entail a certain justice cost: "valid defenses and counterclaims will be sacrificed by defendants under great pressure to get the lien released, and claims will be settled for an amount higher than that which the plaintiff would expect to get at trial".[540]

The method of attachment employed also will have an impact on the fortunes of creditors. Physical seizure of a debtor's property will provide the creditor with "absolute security for the satisfaction of an eventual judgment by placing property safely in the hands of a disinterested third party".[541] A system of prejudgment attachment based on notional seizure or registration, on the other hand, may increase the creditor's risk while minimizing the hardship of attachment for the debtor. In some cases, injunctive relief will provide the creditor with adequate protection and still allow the debtor to enjoy his property.

The degree of protection that creditors are afforded by prejudgment attachment also entails certain societal costs. The less control that a debtor subject to attachment is allowed to have over his property before judgment, the more his creditor will be relieved of the expense of monitoring the actions of the debtor. Costly voidable transactions litigation may be the result of a method of attachment that inadequately safeguards the interests of creditors.

At the present time, attachment under Ontario's absconding debtors legislation is effected in the same manner as execution, that is to say, by seizure of the attached property.[542] In addition, as was stated earlier,[543] prejudgment garnishment was available in the small claims courts until 1977. For the last few years, as a result of the advent of the *Mareva* injunction jurisdiction, a creditor has also been able to ask a court to restrain a debtor from dealing with his assets to the creditor's detriment prior to judgment.

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[538] *Ibid.*, at 836.

[539] See Albert, "Attachment in California: A New Look at an Old Writ" (1969-70), 22 Stan. L. Rev. 1254.

[540] *Ibid.*, at 1260.

[541] Zaretsky, *supra*, note 537, at 825.

[542] See the *Absconding Debtors Act*, *supra*, note 44, s. 7, and the *Small Claims Courts Act*, *supra*, note 45, s. 159.

[543] See *supra*, sec. 2(b)(ii)a.

The Rules respecting the method of enforcing an order of attachment in Nova Scotia and Prince Edward Island are undoubtedly the most comprehensive in Canada. Three different methods of attachment are employed under these Rules, depending on the type of property sought to be attached. The general method of attachment prescribed is physical seizure. However, the Rules also provide that, in certain circumstances, attachment can be effected only by registration[544] or service of an order of attachment.[545] Moreover, in both Provinces, Rule 49.04(1)(e)(i) provides that, unless the sheriff receives written instructions from the creditor for the physical seizure of the attached property, the sheriff must "leave the property in the place where it was attached in the custody of the defendant or person in whose possession it had been at the time of attachment, as the sheriff's agent". This would be equivalent to "walking possession" under the Commission's recommendations regarding postjudgment enforcement.[546]

The California attachment legislation is even more detailed than that in Nova Scotia and Prince Edward Island. The method of attachment required to be employed varies with the type of property involved. Real property, for example, is secured by registration of the necessary documentation in the appropriate court office and service of a copy of the documents upon the debtor.[547] Tangible property in the possession of the debtor must be taken into custody by the levying officer.[548] Where such property is in the hands of a person other than the debtor, on the other hand, it is attached by service of a copy of the writ and notice of attachment on such person.[549]

Special provision is made for the attachment of the equipment, products or inventory, and motor vehicles and vessels of an ongoing business, with a view to minimizing the disruptive effect of prejudgment attachment.[550] In each case, attachment by registration is permitted, leaving the property in the control of the debtor. Section 488.350 of the California Code of Civil Procedure, concerned with motor vehicles and vessels of an ongoing business, provides the creditor with protection against questionable dealings with such property. However, "the rights of a person who is a bona fide purchaser of the vehicle or vessel and obtains possession of both the vehicle or vessel and its certificate of ownership"[551] are unaffected by attachment. In the case of the products and inventory of an ongoing business, section 488.360(c) of the California Code of Civil Procedure notes that registration "provides the plaintiff with the same rights and priorities in the attached property as would be obtained by a secured party who perfects interest . . . in such property by filing a financing statement". In other words, the creditor in such a case would enjoy all the rights and privileges accorded a secured party under the California equivalent of the Ontario *Personal Property Security Act*.[552]

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[544] In the case of real property, see Nova Scotia Rules, r. 49.04(1)(g), and Prince Edward Island Rules, r. 49.04(1)(g).

[545] In the case of shares, bonds, debentures or other interests in a body corporate, see Nova Scotia Rules, r. 49.07, and Prince Edward Island Rules, r. 49.07. In the case of property in the possession of a third party, see Nova Scotia Rules, r. 49.04(1)(f), and Prince Edward Island Rules, r. 49.04(1)(f).

[546] See Commission Report, *supra*, note 1, Part II, ch. 2, at 113-19.

[547] West's Cal. Code Civ. Pro. (1982), §488.310. Effective July 1, 1983, a new Article 2 would govern the methods of attachment: see *supra*, note 386.

[548] *Ibid.*, §488.320.

[549] *Ibid.*, §488.330.

[550] *Ibid.*, §488.340 (equipment); §488.350 (motor vehicles and vessels); §488.360 (products and inventory).

It will be recalled that a creditor employing either the noticed hearing procedure or the *ex parte* procedure under the California Code also may obtain from the court a temporary protective order.[553] Service of such an order creates a lien on the debtor's property and, by virtue of section 486.110, this lien is valid against all the world except a *bona fide* purchaser or encumbrancer for present value or a transferee in the ordinary course of business. Again, we see a legislative attempt to balance the creditor's need for protection before judgment against the interest of his debtor in being able to deal with his property fairly.

The English courts, in developing the *Mareva* injunction, have attempted a similar balance. While prejudgment injunctive relief leaves the debtor's property in the debtor's hands pending the final determination of the dispute, his right to deal with his property is restricted substantially.[554] Compliance with a *Mareva* injunction is guaranteed by the fact that contravention would result in contempt proceedings and possible imprisonment.

The recent decision of Robert Goff J., in *Iraqi Ministry of Defence v. Arcepey Shipping Co. SA*,[555] is indicative of the balancing approach that the English courts have adopted with respect to prejudgment relief. In that case, certain creditors sought to vary a *Mareva* injunction, which had been granted to another of their debtor's creditors, in order to permit the debtor to pay the applicants' outstanding claims. His Lordship granted the application since, in his view, the purpose of a *Mareva* injunction was not to prohibit the debtor from dealing *bona fide* with his property, but simply to prevent the debtor from disposing of his property with intent to defeat a creditor's claim.

In considering the method of attachment most likely to effectuate the security function of the remedy of prejudgment attachment at minimum cost to creditors, debtors, and society as a whole, the Commission has been impressed by the need for flexibility. In some cases, physical seizure may allow this goal to be realized; in other cases, the interests of the creditor and his debtor will best be served by some type of notional seizure or an order enjoining the debtor from dealing with his property in certain ways.

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[551] *Ibid.*, §488.350(d).

[552] *Personal Property Security Act*, R.S.O. 1980, c. 375.

[553] See discussion *supra*, sec. 6(b)(ii)a.

[554] See, however, the recent case of *C.B.S. United Kingdom Ltd. v. Lambert*, [1982] 3 W.L.R. 746, [1982] 3 All E.R. 237 (C.A.), where the Court ordered that the assets of the defendant "be delivered up" pending trial.

[555] *Supra*, note 274.

We do not believe that a single method of attachment is capable of ensuring that the interests of creditors and debtors will be balanced in every case. In the Commission's opinion, in order to create a system of prejudgment attachment that will be responsive to the needs of both debtors and creditors, the authority responsible for the granting of this relief must be given broad discretion to determine the means of attachment that should be employed, having regard to the circumstances of the particular case and the type of property sought to be attached. Then, if the creditor's interests can be served by a notional seizure (or "walking possession") of his debtor's property or by way of a prejudgment injunction, it can so be ordered. Where physical seizure is required to ensure the payment of a future judgment, this method of attachment may be ordered. Indeed, different kinds of the debtor's property may require that more than one method of attachment be employed.

Accordingly, subject to our recommendation relating to the attachment of realty, the Commission recommends that the issuing authority should have a broad discretion to order any method or methods of attachment it considers just and equitable, having regard to all the circumstances of the case, including the type of property sought to be attached and the desirability of avoiding hardship to the parties or any interested person. In particular, it should be possible to order physical seizure, "walking possession", registration of the order under the *Personal Property Security Act*, and attachment by injunction. We turn now to a discussion of these methods of attachment.

Where physical or notional seizure (or "walking possession") is ordered, it should be effected in the same manner as postjudgment seizure, and the Commission's proposals respecting the postjudgment seizure of a judgment debtor's personal property should apply equally to prejudgment seizure of such property, and we so recommend.[556]

However, we also believe that it should be possible to order attachment of a debtor's personal property by registering a copy of an attachment order in the security register established under the *Personal Property Security Act*. The purpose of such registration would be to "bind" the debtor's property, not to give the attaching creditor a right of priority to the property or proceeds thereof *vis-à-vis* other unsecured creditors of the debtor, whether they be judgment or non-judgment creditors. In this respect, registration of an attachment order under the *Personal Property Security Act* would have the same effect as a *Mareva* injunction.[557] However, registration would give the creditor a higher claim to the goods than a subsequent encumbrancer or purchaser of the goods, except where the property is sold in the ordinary course of business.[558] Consequently, the debtor's ability to defeat the creditor's claim by disposing of his property would be considerably restricted. Since the *Personal Property Security Act* is designed to accommodate primarily voluntary security agreements, the Act and the register would have to be modified to comprehend the involuntary security arrangements resulting from prejudgment attachment.

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[556] See ch. 2 of Part II of the Commission's Report, *supra*, note 1.

[557] See *supra*, sec. 3(a).

Among the advantages of attachment by registration are the following. First, the debtor would continue to have the use of his property. Secondly, the registration of attachment orders would provide prospective creditors of the debtor, purchasers of the attached property, and other interested parties with greater protection, since information about the debtor and his financial circumstances would be much more readily ascertainable. Thirdly, since the attached property would remain in the hands of the debtor until judgment, it is unlikely that attachment would continue to provide a creditor with the degree of leverage traditionally ascribed to attachment by physical seizure of the debtor's property. Fourthly, where attachment by registration is appropriate, we believe substantial costs can be saved, such as storage costs and the fees of the enforcement office. We are of the view that a system of attachment by registration will increase the efficiency of provisional relief, since it is likely to reduce debtor objections and resort to the judicial system.

It may be contended that a system of attachment by registration under the *Personal Property Security Act* would be somewhat anomalous in light of some of the Commission's earlier decisions concerning postjudgment seizure of a debtor's property. For example, we proposed in chapter 2 of Part II of the *Report on the Enforcement of Judgment Debts and Related Matters* that the binding of a judgment debtor's personal property should be effected by the delivery of a writ of enforcement to the new enforcement office.[559] In addition, we recommended that no person who acquires his title from the debtor should be prejudiced by the commencement of enforcement activities and the consequent binding of the debtor's property, so long as he acquires the title in good faith, for valuable consideration, and without actual notice of the delivery of a writ of enforcement to the new enforcement office.[560] Registration of an attachment order under the *Personal Property Security Act*, on the other hand, would constitute notice to all the world, and a subsequent purchaser or encumbrancer of attached property would take at his own risk.[561] Consequently, a judgment creditor would be afforded less protection than an attaching creditor.

While we acknowledge that such a result may well seem somewhat irregular, nevertheless, the Commission is of the opinion that a system of attachment by registration is defensible. It must be recognized that a registration system is a compromise solution. While an attaching creditor who files a copy of an attachment order under the *Personal Property Security Act* may enjoy greater protection than a judgment creditor who delivers a writ of enforcement to the new enforcement office, the two situations are not really comparable. A judgment creditor always has the option of instructing the enforcement office to seize his debtor's property, thereby gaining maximum security for his judgment. An attaching creditor who must proceed against his debtor's property by way of registration has no similar choice. His right of seizure has been curtailed in an effort to reduce the risk to his debtor from prejudgment relief.

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[558] See *Personal Property Security Act*, *supra*, note 552, s. 30(1).

[559] For a discussion of the new enforcement office, see Commission Report, *supra*, note 1, Part I, ch. 3, at 123-24.

[560] This recommendation would mean that the *bona fide* purchaser for value without notice exception now found in s. 10(1) of the *Execution Act*, R.S.O. 1980, c. 146, would be retained under the new law of enforcement.

[561] *Supra*, note 552, s. 53.

Regarding the position of third parties in a system of attachment by registration, again it may be argued that it is unusual that a purchaser of property should be in a more precarious position where an attachment order has been issued than if judgment has been granted and a writ of enforcement filed with the enforcement office. Whereas a purchaser would take subject to a writ of enforcement only if he had actual notice of the writ, he would be bound by an attachment that is registered, regardless of whether he had actual notice, unless, for example, the property were sold in the ordinary course of business.

Although the risk to a purchaser or encumbrancer would be increased where an attachment order is registered in the personal property security register, this result does not seem unreasonable given the beneficial purpose of a system of prejudgment attachment by registration. Moreover, such a system is unlikely to add to the onus of a purchaser or encumbrancer. Where a purchaser now would conduct a search of the personal property security register, he would do so irrespective of the registration of attachment orders; where he now would conduct no search, the registration of attachment orders is unlikely to result in a change in practice. Accordingly, the Commission has concluded that it should be possible to order attachment of a debtor's personal property by registering a copy of the attachment order in the personal property security register. To this end, we recommend that the *Personal Property Security Act* should be amended to accommodate attachment by registration.

Because of the adverse effect that registration of an attachment order in the personal property security register may have on the debtor's creditworthiness, we believe that the attaching creditor should be under a duty to have the registration deleted if he is no longer entitled to the attachment order—for example, where the creditor has been paid or where the attachment has been discharged or dissolved.[562] Failure to do so should result in the creditor's liability for any damages that the debtor may suffer as a consequence. We so recommend.

Another method of attachment that should be available in the Commission's opinion is "attachment" by injunction. In some cases, prejudgment injunctive relief, whether alone or in conjunction with another method of attachment, will be the most equitable way in which to secure a debtor's property. Attachment by registration may inhibit the disposition of property by the debtor; however, it would not prevent the debtor from concealing his property or removing it from the jurisdiction. In such a case, attachment by way of an injunction might be useful; the debtor would be able to continue to use and enjoy his property pending final judgment, while the threat of contempt proceedings and possible imprisonment would encourage compliance.

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[562] See *infra*, sec. 7(i)(vi).

With respect to realty, we are of the view that registration of a copy of an attachment order in the appropriate land registry office should be the only method of attachment available to creditors. This would be in accordance with the thrust of the Commission's short term and long term proposals for enforcement against land after judgment, as set out in Part III of our *Report on the Enforcement of Judgment Debts and Related Matters*, which are based on a belief that the present system of filing writs of execution in the sheriff's office and land titles office gives rise to costly conveyancing problems, and therefore is highly inefficient.

Registration of an attachment order against the debtor's title to land would guarantee payment of any future judgment that the creditor might obtain against the debtor. This method of attachment also would allow the debtor to continue to use and enjoy his property prior to the final adjudication of the creditor's claim. Therefore, we recommend that, in the case of realty, attachment should be required to be effected by the registration of a copy of an attachment order against the title of the debtor's property pursuant to the terms of the *Registry Act*[563] or the *Land Titles Act*,[564] which should be amended to accommodate the registration of such orders.

(l) PROCEDURAL SAFEGUARDS

To this point in our discussion, the focus has been on substantive aspects of the new law of attachment. However, in order to achieve a proper balancing of the interests of creditors and debtors, adequate procedural safeguards also must be built into the law. It is to the subject of such safeguards that we now turn our attention.

(i) The Application for Prejudgment Attachment

Proof of entitlement to an attachment order is one of the areas in which Ontario's existing absconding debtors legislation is woefully inadequate. While section 3(1) of the *Absconding Debtors Act* does require an attaching creditor to state that he has "good reason to believe and does believe" that the debtor has absconded with the requisite intent, it would seem that the creditor need not state the grounds for his belief. Of even greater significance is the fact that, under this Act, a creditor may secure an order of attachment without establishing that he has a reasonable chance of succeeding in his action against the debtor. The evidentiary requirements of the absconding debtors provisions of the *Small Claims*

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[563] R.S.O. 1980, c. 445.

[564] R.S.O. 1980, c. 230.

Courts Act are no more onerous.[565]

The evidentiary requirements of most modern attachment legislation is substantially more exacting. For example, Rule 49.02 of the Nova Scotia Rules provides as follows:

> 49.02. The affidavit of a plaintiff or his agent in support of an attachment order shall,
>
> (a) set out facts showing
>
> (i) the plaintiff has a good cause of action against a defendant whose property is to be attached, and
>
> (ii) the existence of one or more grounds of attachment as set out in rule 49.01(1);
>
> (b) state the amount of the claim that the plaintiff seeks to recover from the defendant, including the amount of probable costs, after allowing for all just credits, set-offs and counter-claims known to him; and
>
> (c) state he was advised by the plaintiff's solicitor, naming him, and verily believes he is lawfully entitled to attach the property.

Similarly, under New York's attachment rules, before a creditor will be entitled to attach his debtor's property, he must show "that there is a cause of action, that it is probable that [he] will succeed on the merits, that one or more grounds for attachment . . . exist, and that the amount demanded from the defendant exceeds all counterclaims known to the plaintiff".[566]

The Commission believes that, in order to prevent abuse, more must be required of an applicant for attachment than a statement of his belief in the existence of some ground for attachment. In our opinion, a creditor applying for prejudgment attachment should be required to show not only that grounds for relief exist, but also that he is likely to succeed in his action against the debtor. It is only where a future judgment against the debtor is probable that prejudgment attachment can be justified.

Just how strong the creditor's case against the debtor must be varies from jurisdiction to jurisdiction. For example, under the Nova Scotia Rules and the Prince Edward Island Rules, the creditor must establish that he has a "good cause of action" against the debtor.[567] Under the New York[568] and California attachment provisions,[569] before a court will grant prejudgment relief it must be satisfied of the "probable" validity of the creditor's claim. Courts, in exercising the *Mareva* jurisdiction, require an applicant for prejudgment injunctive relief to establish that he has a "good arguable case" or "a strong *prima facie* case" against the debtor.[570]

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[565] See s. 159 of the *Small Claims Courts Act*, *supra*, note 45, and the form of affidavit for attachment against an absconding debtor, Form 57, prescribed by the small claims courts Rules of Procedure, R.R.O. 1980, Reg. 917.

[566] N.Y. Civ. Prac. Law §6212(a) (McKinney).

[567] See r. 49.02(a)(i) of both the Nova Scotia Rules and Prince Edward Island Rules.

[568] N.Y. Civ. Prac. Law §6212(a) (McKinney).

[569] West's Cal. Code Civ. Pro. (1982), §§484.030 and 484.090(a)(2).

While any one of these tests would protect debtors satisfactorily against overreaching creditors, for two reasons the Commission prefers the "strong *prima facie* case" test that is now sometimes employed in respect of interlocutory injunction applications under section 19(1) of the *Judicature Act*,[571] and that was recently adopted for *Mareva* injunction applications in particular by the Ontario Court of Appeal.[572] First, we believe that this measure of the strength of the creditor's case will result in a proper balancing of the interests of debtors and creditors. And secondly, this standard, unlike the others set out above, is well known to practitioners and to the judiciary in Ontario.

Having regard to the risks inherent in attachment, the Commission is of the opinion that two additional safeguards should be built in to the procedure at the initial stage. It seems only just and equitable that a creditor should be allowed to attach sufficient of the debtor's property to secure his ultimate judgment against the debtor, but no more. Therefore, we believe that a creditor's application for relief should indicate the amount that he seeks to recover from the debtor over and above all set-offs and counterclaims known to the creditor. To allow a creditor to attach property of his debtor in excess of this figure would go beyond the purpose of a prejudgment remedy. Some such limitation on prejudgment attachment exists in a number of jurisdictions.[573]

As a further deterrent against possible abuse of the remedy of prejudgment attachment, we advocate that every person seeking such relief should be required to swear under oath that his application is made *bona fide* for the sole purpose of obtaining security for the enforcement of any future judgment against the debtor in the main action. Because of the possibility of perjury charges, this formality may cause some creditors, whose real motive is to coerce debtors to settle, to reconsider resort to prejudgment attachment.[574]

Accordingly, the Commission recommends that attachment should be available only after the creditor has established under oath the existence of one or more grounds for attachment and a strong *prima facie* case against the debtor, and has affirmed the amount that he seeks to recover from the debtor over and above all set-offs and counterclaims known to him, and that his application for prejudgment attachment is made *bona fide* for the sole purpose of obtaining security for the enforcement of any future judgment against the debtor in the main action.

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[570] See discussion *supra*, secs. 3(a) and (b). The former is the test used in England; the latter is the test adopted recently by the Ontario Court of Appeal in *Chitel v. Rothbart*, unreported (December 2, 1982, Ont. C.A.).

[571] See Sharpe, "Interlocutory Injunctions: The Post-American Cyanamid Position", in Gertner (ed.), *Studies in Civil Procedure* (1979), at 188-90.

[572] See *Chitel v. Rothbart*, *supra*, note 570.

[573] See Nova Scotia Rules, r. 49.02(b); Prince Edward Island Rules, r. 49.02(b); Manitoba Queen's Bench Rules, *supra*, note 89, r. 583(d); N.Y. Civ. Prac. Law §6212(a) (McKinney); and West's Cal. Code Civ. Pro. (1982), §484.020(b).

[574] See West's Cal. Code Civ. Pro. (1982), §484.020(c).

(ii) The Issuing Authority

Having determined what every applicant for attachment must prove, the question arises upon whom the responsibility for granting such relief should fall. In answering this question, we have considered two options, both employed at present in Ontario. Under section 3(1) of the *Absconding Debtors Act*, the authority to grant an order of attachment is vested in the judges of the Supreme Court and county and district courts.[575] Section 159 of the *Small Claims Courts Act*, on the other hand, empowers the clerk of a small claims court to issue a warrant of attachment.[576]

We are of the opinion that prejudgment attachment is a matter that requires judicial supervision in all cases. The fact that a creditor's claim is one within the monetary jurisdiction of the small claims courts does not mean that the harm the debtor might suffer as a result will necessarily be minor. Indeed, the consequences of attachment may be most severe in the case of a debtor with little or no financial cushion upon which to fall back. Moreover, we believe that a judge, rather than a clerk or some other administrative official, is the person most suited to make the kinds of determination necessitated by our proposals regarding the grounds for attachment.

Among other Canadian jurisdictions, at the present time, prejudgment attachment is left in the hands of quasi-judicial or administrative officials in only two provinces: Nova Scotia and Prince Edward Island.[577] The attachment legislation in all three American jurisdictions that we have examined has given courts the power to order prejudgment attachment, and the United States Supreme Court has emphasized the importance of judicial supervision in the provisional relief context.[578] Given the nature of prejudgment attachment, the Commission recommends that the jurisdiction to grant such relief should be exercised by a judge.

(iii) Notice of Prejudgment Attachment Proceedings

Under existing Canadian attachment and absconding debtors legislation, an application for prejudgment attachment may be heard *ex parte*;[579] in other words, the debtor need not be given notice of the creditor's application for provisional relief, nor an opportunity to be heard before the relief requested is granted. This is certainly the case with the Ontario *Absconding Debtors Act* and the absconding debtors provisions of the *Small Claims Courts Act*. The absence of a notice requirement in provisional relief legislation in Canada is in sharp contrast to recent legislative developments in the United States.

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[575] The forum chosen will depend, of course, on the amount claimed by the creditor.

[576] It should be noted that a creditor is given the option of applying to a judge or a justice of the peace for a warrant of attachment under s. 160 of the *Small Claims Courts Act*, *supra*, note 45. "Judge" is defined for the purposes of this Act as "a small claims court judge" or "a judge of a county court": see s. 1(*h*).

[577] See r. 49.01(2) of both the Nova Scotia Rules and the Prince Edward Island Rules.

[578] See *Sniadach v. Family Finance Corp. of Bay View*, *supra*, note 372; *Fuentes v. Shevin*, *supra*, note 377; *Mitchell v. W.T. Grant Co.*, *supra*, note 380; and *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, *supra*, note 382.

In response to the due process pronouncements of the United States Supreme Court in *Sniadach v. Family Finance Corp. of Bay View* and subsequent cases,[580] both New York and California introduced a noticed hearing procedure for the determination of prejudgment attachment applications.[581] Although in neither case is notice to the debtor obligatory, the legislation does put a premium on the use of the noticed hearing procedure. For example, under section 6211(b) of the New York Civil Practice Law and Rules, a creditor who obtains an *ex parte* order of attachment must move for an order confirming the order of attachment "within a period not to exceed five days after levy". To obtain an *ex parte* writ of attachment under the California Code of Civil Procedure, a creditor must be able to satisfy the court "that great or irreparable injury would result . . . if issuance . . . were delayed until the matter could be heard on notice".[582]

In the context of the attachment laws of California and New York, a noticed hearing procedure is understandable. In each case, a creditor may resort to prejudgment attachment in other than extraordinary circumstances; for example, under section 6201 of the New York Civil Practice Law and Rules, attachment is available where the debtor is a nondomiciliary residing without the state or where the creditor's claim is based "on a judgment, decree or order of a court of the United States . . . which is entitled to full faith and credit". This Commission, on the other hand, has sought to restrict the prejudgment remedy of attachment to exceptional circumstances. Under the proposed grounds for attachment,[583] the imposition of a requirement that the creditor notify his debtor of the impending attachment application would put the creditor unjustifiably at substantial risk. The procedural safeguards recommended above, as well as those to be discussed below, we believe, will ensure that the law takes sufficient cognizance of the debtor's interests.

Accordingly, we recommend that prejudgment attachment should continue to be available upon the *ex parte* application of a creditor. To provide the debtor with additional protection where an order of attachment has been obtained on an *ex parte* basis, however, we are of the view that the order should be granted for a limited period of time and that the attaching creditor should be required to return to court to seek a continuation of the attachment order if he wishes to have the order continue to bind the debtor's property. In other words, an *ex parte* attachment order would be similar to an *ex parte* injunction granted for a limited period of time.[584] We also believe that the onus should continue to be on the creditor upon a return of the motion to satisfy the court that there are grounds for prejudgment attachment. We so recommend.

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[579] For example, this practice is sanctioned expressly by the Alberta Rules of Court, *supra*, note 89, r. 485; Nova Scotia Rules, r. 49.01(2); Prince Edward Island Rules, r. 49.01(2); and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 3(1).

[580] See *supra*, note 578.

[581] See N.Y. Civ. Prac. Law §6210 (McKinney), and West's Cal. Code Civ. Pro. (1982), §§484.010 *et seq*.

[582] West's Cal. Code Civ. Pro. (1982), §485.010(a). The same requirement must be satisfied in order to obtain an *ex parte* temporary protective order under the California Code: see §486.010.

[583] See discussion *supra*, sec. 7(c)(i).

We also believe that a debtor whose property is attached should be provided with sufficient information to allow him to meet the creditor's request for a continuation of an attachment or to mount a challenge to the validity of the court's order. Therefore, the Commission recommends that the debtor should be served with a copy of the attachment order together with a copy of the material supporting the creditor's application for prejudgment attachment.

We return below to the rights of a debtor whose property has been attached to dispute the attachment order.[585]

(iv) The Creditor's Bond or Undertaking

Prejudgment attachment legislation in many jurisdictions imposes an obligation on the attaching creditor to file a bond or undertaking as a precondition to obtaining the relief requested. The purpose of such a requirement is really twofold. First, it is likely to discourage creditor abuse of the prejudgment remedy of attachment. A creditor who recognizes that he runs a serious financial risk by resorting to attachment in cases where such relief may not be justified probably will be unwilling to do so. Secondly, the creditor's bond or undertaking helps to ensure that a debtor or other person who is injured by reason of an attachment order will be able to recover damages for such injury in appropriate circumstances.

Debtors in Ontario are afforded no such protection at the present time. Neither the *Absconding Debtors Act* nor the absconding debtors provisions of the *Small Claims Courts Act* obligate a creditor seeking prejudgment attachment to file a bond or undertaking as a precondition to the obtaining of such relief. Both Acts, however, do require a bond to be filed with the sheriff or bailiff, as the case may be, if the creditor wishes to secure the sale of perishable property that has been attached.[586]

The Ontario position may be contrasted with the position under the

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[584] See Williston and Rolls, *The Law of Civil Procedure* (1970), Vol. 2, at 594-97.

[585] See *infra*, sec. 7(i)(vi).

[586] See the *Absconding Debtors Act*, *supra*, note 44, s. 8, and the *Small Claims Courts Act*, *supra*, note 45, s. 172. It should be noted that s. 172 of the *Small Claims Courts Act* also authorizes a bailiff to refuse to attach perishable property until he is provided with a bond by the attaching creditor.

Nova Scotia Rules and the Prince Edward Island Rules. Each makes the issuance of an attachment order conditional upon the receipt of a bond in an amount equal to one and one quarter times the value of the property sought to be attached.[587] Rule 49.03(2) of both the Nova Scotia Rules and the Prince Edward Island Rules requires the conditions of the creditor's bond to be the following:

> (a) [that] the plaintiff shall prosecute the proceeding without delay to judgment; and
>
> (b) [that] when ordered by the court,
>
> (i) the sheriff shall return the attached property, or the proceeds thereof if sold . . . to the defendant or other person from whom it was attached, and
>
> (ii) the plaintiff shall pay to the defendant or other person the damages and costs that either of them has sustained by reason of the wrongful issue of the attachment order, or the wrongful making of any attachment thereunder, or if the plaintiff fails to recover judgment against the defendant in the proceeding, or as the court may order.

While a bond would seem to be the most common form of security provided by creditors under these Rules, it should be noted that other forms of sufficient security may be approved.

A somewhat different approach has been adopted in California and New York. In each state, the courts responsible for the granting of prejudgment attachment are given a broad discretion regarding the amount of the undertaking that an attaching creditor must give. Section 6212(b) of the New York Civil Practice Law and Rules provides that the creditor must give an undertaking "in a total amount fixed by the court, but not less than five hundred dollars"; section 489.220(b) of the California Code of Civil Procedure states that the court may order the undertaking to be in such amount as "it determines to be the probable recovery for wrongful attachment if it is ultimately determined that the attachment was wrongful".

The Commission is of the view that the security provisions of Ontario's present absconding debtors legislation are seriously deficient. At best, they may prevent an uncalled for sale of property that is perishable in nature. However, they would appear to do little to protect a debtor from improper reliance by his creditors upon prejudgment attachment. Later in this chapter, we shall recommend that a person injured by reason of a wrongful attachment should have a cause of action against the attaching creditor.[588] To give force to this recommendation, we believe that, as a prerequisite to attachment, every attaching creditor should be required either to post a bond or to give an undertaking in respect of any damages that his debtor may suffer as the result of an unwarranted attachment order.[589] It is the opinion of the Commission that, in order to ensure that justice is done, the court granting the creditor's request for an attachment order should be empowered, regardless of the circumstances of the case, to fix the amount of the creditor's bond or undertaking, so as to cover the plaintiff's probable liability for wrongful attachment. The Commission prefers this approach to that of fixing the amount of the bond or undertaking by a multiple of the value of the property attached for the simple reason that, in our opinion, there is no necessary correlation between the value of the attached property and the damages likely to be suffered by the debtor. Accordingly, we recommend that the issuance of an attachment order should be dependent upon the attaching creditor posting a bond or giving an undertaking in an amount, to be determined by the court, that will cover the plaintiff's probable liability for wrongful attachment.

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[587] See r. 49.03(1) of both the Nova Scotia Rules and the Prince Edward Island Rules.

[588] See *infra*, sec. 7(k).

This last recommendation would enure to the benefit of, not only the debtor, but also a third party affected by an attachment order who may suffer damages as a result thereof. However, a third party may also be put to certain expenses in order to ensure compliance with an order. Since the third party will normally be a stranger to the dispute between the creditor and the debtor, we do not believe that he should be prejudiced thereby. Accordingly, the Commission recommends that, as a precondition to the making of an attachment order, the attaching creditor should be required to undertake to pay the costs incurred by the third party as a result of an order of attachment. It will be recalled that the English courts have imposed a similar obligation on a party seeking a *Mareva* injunction.[590]

(v) The Debtor's Right to Provide Alternative Security

Yet another method that may be used to safeguard the interests of debtors in the prejudgment relief context is to allow a debtor whose property has been attached to provide his creditor with alternative security for his future judgment. Under section 12(1) of the Ontario *Absconding Debtors Act* and section 169(1) of the *Small Claims Courts Act*, a debtor who files a bond with sufficient securities in double the appraised value of the property attached may apply to have his property restored to him. Neither Ontario Act, however, allows a debtor to provide his creditor with alternative property, and in this way regain possession of his property.[591]

More liberal legislation is to be found in a number of the other provinces. For example, the Saskatchewan *Absconding Debtors Act*[592] authorizes the sheriff to restore any attached property where he is given sufficient security for an amount equal to its appraised value or where such an amount is paid into court. The Nova Scotia Rules and the Prince Edward Island Rules permit restoration of attached property upon receipt by the prothonotary or the sheriff of a bond equal to one and one quarter times the valuation of the attached property, or of some other form of sufficient security sanctioned by the prothonotary.[593]

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[589] The undertaking contemplated by the Commission would be similar to that provided by a person applying for an interlocutory injunction: see Sharpe, "Interlocutory Injunctions: The Post-American Cyanamid Position", in Gertner (ed.), *Studies in Civil Procedure* (1979), at 191-92. Such an undertaking now is required in the case of a *Mareva* injunction: see, for example, *Third Chandris Shipping Corp. v. Unimarine SA*, *supra*, note 262, at 985.

[590] See *supra*, sec. 3(a).

[591] For similar legislation in other provinces, see the Manitoba Queen's Bench Rules, *supra*, note 89, r. 601, and *The Judicature Act*, R.S.N. 1970, c. 187, s. 83.

[592] R.S.S. 1978, c. A-2, s. 6. See, also, the Alberta Rules of Court, *supra*, note 89, r. 488, and the *Code of Civil Procedure*, R.S.Q. 1977, c. C-25, art. 739.

We too favour allowing a debtor to apply to the court for a return of his property where the debtor is able to provide the creditor with adequate, alternative security. As long as the creditor's prejudgment security is adequate, the nature of the security would seem to be immaterial to the creditor. On the other hand, the property attached may be extremely important to the debtor; for example, it may be a piece of equipment that is crucial to the debtor's business. In such circumstances, there would seem to be every reason to permit the debtor to substitute one type of security for another, and no reason to deny it. We also believe that the interests of debtors can be served better by giving courts a broad discretion to decide whether the alternative security offered is adequate, rather than invariably requiring debtors to file a bond in an amount that is a multiple of the appraised value of the attached property. Finally, we are of the opinion that, not only should the debtor be allowed to regain possession of his property in the manner described above, but any person affected by an attachment order should have the same right. In this way, the impact of attachment proceedings on third persons can be minimized.[594] Consequently, the Commission recommends that the court should be empowered to order the release of any property attached and its restoration to the debtor or to any person entitled thereto, upon the receipt of substitute security that, in the opinion of the court, is adequate.

The preceding discussion is based on an assumption that the debtor's property has been attached by means of physical seizure. However, this will not always be the case. It will be recalled that the Commission has recommended that, generally speaking, a debtor's assets should be capable of being attached in a number of different ways, including physical seizure, registration of the order of attachment in the *Personal Property Security Act* register, or by way of an injunction.[595] The Commission believes that, no matter what method or methods of attachment are employed, the right to substitute other property for the attached property should be available, and we so recommend.

(vi) Dissolution, Variation, Modification, and Discharge of an Attachment Order

In a previous section,[596] we considered whether a debtor should be entitled to notice of his creditor's application for prejudgment attachment and an opportunity to be heard before the making of an attachment order. The Commission rejected any such notice requirement, and recommended that an attachment order should be available on an *ex parte* application. However, the creditor would be required, within the time specified by the court, to seek a continuation of the *ex parte* order, and to serve the debtor with a copy of the attachment order together with a copy of the material supporting the creditor's application. Upon a return of the motion, the debtor would be able to contest the creditor's application.[597] Despite these safeguards, we believe that debtors must be afforded certain other procedural protections, such as the right to apply for a dissolution of the attachment order, either before or after the continuation hearing, or for a variation, modification, or discharge of the attachment order. We turn now to consider the abovementioned procedural protections.

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[593] See r. 49.06 of both the Nova Scotia Rules and the Prince Edward Island Rules.

[594] See, for example, r. 49.06 of both the Nova Scotia Rules and the Prince Edward Island Rules. See, also, r. 488 of the Alberta Rules of Court, *supra*, note 89, and *The Absconding Debtors Act*, R.S.S. 1978, c. A-2, s. 6.

[595] See *supra*, sec 7(h).

[596] See *supra*, sec. 7(i)(iii).

Once again, the Ontario *Absconding Debtors Act* and the absconding debtors provisions of the *Small Claims Courts Act* are wanting in these areas. Neither statute expressly authorizes a debtor to move for the immediate dissolution of an attachment order. While there are examples of cases in which a debtor has successfully brought an application to set aside an order of attachment,[598] we are of the opinion that the right of a debtor to apply to have an attachment order dissolved or set aside should be prescribed by statute. Accordingly, we recommend that a debtor against whom an attachment order has been issued should be entitled to apply, in accordance with the rules of civil procedure, for the dissolution of the order.[599]

As in the case of the power to dissolve or set aside an attachment order, both the *Absconding Debtors Act* and the *Small Claims Courts Act* are silent concerning the power of the court to vary, modify, or discharge such an order. This state of affairs may be contrasted with the position in a number of other Canadian provinces and in some American jurisdictions. Rule 49.12(c) of both the Nova Scotia Rules and the Prince Edward Island Rules, for instance, expressly authorizes the court, upon application, to vacate in whole or in part an attachment order, and any attachment made thereunder, where it is satisfied "that the attachment order is not necessary for the security of a plaintiff, or a plaintiff has failed to bring the proceeding to trial and judgment promptly,[600] or the proceeding has been discontinued or dismissed as against a defendant, or a plaintiff's claim . . . has been fully satisfied". Under Rule 49.12(b) of both these Rules, a court is empowered to "amend or modify the attachment order or any attachment made thereunder". The attachment provisions found in the New York Civil Practice Law and Rules permit a court to vacate or modify an order of attachment,[601] and provide that an order of attachment is annulled once the action in which it was granted "abates or is discontinued, or a judgment therein in favour of the plaintiff is fully satisfied, or a judgment is entered therein in favour of the defendant".[602]

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[597] *Ibid.*

[598] See *supra*, sec. 2(b)(i)c.(6).

[599] With respect to who should bear the onus of satisfying the court of the existence of one or more grounds of attachment, see §6211(b) of the N.Y. Civ. Prac. Law (McKinney).

[600] Under s. 7(2) of the Saskatchewan *Absconding Debtors Act*, R.S.S. 1978, c. A-2, the court may order the attached property to be returned "[i]f the plaintiff is guilty of unnecessary delay in the prosecution of his suit to judgment".

In the opinion of the Commission, the absence of such a provision or provisions in Ontario's absconding debtors legislation is a serious lacuna, and one that should be corrected in any future attachment legislation. Undoubtedly, there will be a myriad of fact situations in which debtors may be entitled to relief from attachment; for example, a debtor may make partial payment of an outstanding debt. The Commission believes that in such a case a debtor should be able to have the attachment order varied or modified to allow part of the attached property to be released. Another circumstance that may justify relief from attachment is delay on the part of the creditor in pursuing his legal remedy: the financial situation of a debtor should not be allowed to be jeopardized unnecessarily by the dilatory conduct of a creditor in getting his action on for trial.

Although, in order to respond to the exigencies of a great many different situations, the court should have a broad power to vary, modify, or discharge an attachment order, we are of the view that, in this area of the law of prejudgment relief, the courts would benefit from some guidance. Therefore, the Commission recommends that a court should have the power to vary, modify, or discharge an attachment order in the following circumstances: (1) where the creditor has failed to proceed with his action against the debtor with reasonable diligence; (2) where the creditor's action has been discontinued, dismissed, or compromised; (3) where the amount of the creditor's claim has been either reduced or increased; or (4) where other just cause exists. Property that has been attached and is affected by such an order should be restored in accordance with the terms of the order of the court. We envisage that creditors and debtors alike will benefit from the court's broad powers in this regard. Furthermore, we believe that any other person claiming to be interested in any attached property should be able to take advantage of the power of the court to vary, modify, or discharge attachment orders, and we so recommend.

(vii) Attachment and Interpleader

In chapter 5 of Part II of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*, we discussed in considerable detail the procedure to be followed for the resolution of disputes that develop in the course of enforcement proceedings among persons claiming an interest in property. Since similar disputes may arise in the context of prejudgment attachment, it would seem that our earlier recommendations should be equally applicable to the resolution of such disputes.

While existing Ontario absconding debtors legislation offers little or no guidance on this subject, the trend in recently enacted attachment legislation is toward the assimilation of prejudgment and postjudgment enforcement in this respect. This is certainly the case with the Nova Scotia Rules,[603] the Prince Edward Island Rules,[604] the New York Civil Practice Law and Rules,[605] and the California Code of Civil Procedure. The assimilation is most complete under the California Code, section 488.090 of which states that "[a] third person shall claim an interest in personal property attached in the manner provided for third-party claims after levy under execution". Consistent with our desire for uniformity in enforcement proceedings,[606] we recommend that our proposals regarding the resolution of disputes respecting the ownership of property that arise in the course of postjudgment enforcement proceedings should apply *mutatis mutandis* to such disputes in the prejudgment attachment context.

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[601] N.Y. Civ. Prac. Law §6223 (McKinney).

[602] *Ibid.*, §6224. For a somewhat comparable provision in the California Code of Civil Procedure, see West's Cal. Code Civ. Pro. (1982), §488.570.

(viii) The Sale of Attached Property

Earlier in this chapter,[607] we outlined the various methods of prejudgment attachment that should be available to a creditor upon the order of a court. We turn in this section to consider another important question, that is, in what circumstances, if any, the sale of attached property should be permitted. The question is significant for both debtors and creditors, since broad sale powers could seriously prejudice the interests of debtors, while closely circumscribed powers of sale might result in injury to creditors. In some cases, however, sale may be beneficial to the debtor and creditor alike; for example, where the attached property is depreciating rapidly in value.

We already have made mention of the sale powers found in Ontario's absconding debtors legislation. To repeat, under the *Absconding Debtors Act*[608] and the *Small Claims Courts* Act,[609] the sheriff or bailiff, as the case may be, is empowered to sell before judgment any attached property that is perishable in nature.[610] In addition, where a debtor has not timeously filed a bond and applied for restoration of his property, section 12(2) of the *Absconding Debtors Act* authorizes the early sale of "any of the goods and chattels that have been attached, except chattels real, upon such terms as the judge considers just".

The sale provision found in the Nova Scotia Rules and the Prince Edward Island Rules is much more sweeping in nature than those described above. Rule 49.09(1) of both the Nova Scotia and the Prince Edward Island Rules provides as follows:

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[603] R. 49.10(2).

[604] R. 49.10(2).

[605] N.Y. Civ. Prac. Law §6221 (McKinney).

[606] See, generally, Commission Report, *supra*, note 1, especially Part I, at 5 and 77.

[607] See *supra*, sec. 7(h).

[608] *Supra*, note 44, s. 8.

[609] *Supra*, note 45, s. 171.

[610] The language of s. 8 of the *Absconding Debtors Act*, it should be noted, is somewhat broader than that found in s. 171 of the *Small Claims Courts Act*. While the latter refers only to perishable property, the former speaks in terms of "perishable property, or such as from its nature cannot be safely kept or conveniently taken care of". Section 8 of the *Absconding Debtors Act* also provides for the sale of certain livestock ("horses, cattle, sheep or pigs").

> 49.09.-(1) When any attached personal property is likely to perish or materially depreciate in value before the probable termination of the proceeding, or the keeping of the property could result in unreasonable loss or expense, or for other just cause, the court may order the sale or other disposal of all or any part of the property in such manner and upon such terms as are just.

It should be noted that this Rule gives the courts a broad discretion to order the sale of attached personal property at any time. The power to order the sale of property that is likely to depreciate materially, or the keeping of which could result in unjustifiable cost to the parties, together with the courts' involvement in sale proceedings, should help to ensure that justice will be done in every case of prejudgment attachment.

In California, also, the courts have been given extensive powers regarding the sale of property that has been attached. Section 488.530 of the California Code of Civil Procedure states in part as follows:[611]

> 488.530. (a) . . . Upon a showing that the property is perishable or will greatly deteriorate or greatly depreciate in value or *that for some other reason the interests of the parties will be best served thereby*, the court may order that such property be sold or may appoint a receiver or direct the levying officer to take charge of, cultivate, care for, preserve, collect, harvest, pack, or sell such property.

Another interesting feature of the California sale provision is the fact that, under section 488.530(b), the levying officer is empowered to "take any action necessary to preserve the value of the property or sell the property" without judicial approval, if the delay in obtaining a court order would result in a substantial diminution in the value of the attached property. Finally, it should be noted that section 488.530(c) expressly provides that any sale of attached property "shall be made in the same manner that property is sold on execution".

In our opinion, the sale provisions of Ontario's absconding debtors legislation are too narrow in scope. The limited power to order the sale of attached property does not allow the courts to deal effectively with the great variety of cases where a sale may best serve the interests of all concerned. Accordingly, we recommend that the court, upon the application of the debtor, the creditor, the enforcement office, or any person interested in the attached property, and upon notice to all concerned, should be empowered to order the sale or disposition of any property that has been attached where the property is likely to perish or to depreciate materially in value before the probable termination of the creditor's action against the debtor, or where the keeping of the property is likely to result in unreasonable loss or expense, or for any other just cause. It will be noted that this proposal would empower the court to authorize a sale, rather than the sheriff or bailiff, as is now the case under the *Absconding Debtors Act* and the *Small Claims Courts Act*, respectively. In our view, the broader sale power that we recommend should be exercised judicially. We further recommend that costs incurred in a sale or disposition of attached property should be a first charge against the proceeds realized.

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[611] Emphasis added.

The court to which an application for sale is made should be authorized to determine the manner and the terms of any sale, having regard to, *inter alia*, the nature of the attached property and the method of attachment employed to secure the property. The Commission envisages that, in most cases, the court will order sale in the same manner and upon the same terms and conditions that property seized after judgment is proposed to be sold.[612]

While the proposals for the sale of attached property outlined so far will operate satisfactorily in the majority of cases, we believe that Ontario's future attachment legislation should contain a provision similar to section 488.530(b) of the California Code of Civil Procedure. Therefore, the Commission also recommends that, where the value of any attached property would be diminished substantially as a result of any delay in its sale in accordance with the procedure described above, the enforcement office should be authorized to take any reasonable steps necessary to preserve the value of the property, including its sale in the manner recommended for the expeditious sale of property in the course of postjudgment enforcement proceedings.[613] Again, the costs incurred to preserve the value of the property should be a first charge against the property or the proceeds realized on a sale thereof. Finally, in order to enable those interested in the sale of attached property to avoid the costs inherent in an application for sale under the above proposals, it is recommended that the creditor, the debtor whose property has been attached, and any other interested person should be able to consent to the sale by the enforcement office, without court approval, of any attached property before judgment has been handed down in the main action.

(j) THE TERM OF AN ATTACHMENT ORDER

Just as we have given consideration to the period of time for which a writ of enforcement and a notice of garnishment or attachment of wages should be effective,[614] so too have we concerned ourselves with the duration of a prejudgment attachment order. A number of different approaches to this subject are suggested by existing legislation in Ontario and in other jurisdictions.

Section 5 of the Ontario *Absconding Debtors Act* states that an order of attachment "shall remain in force for six months". A sheriff to whom an order of attachment is delivered, therefore, has six months in which to enforce the order. However, section 5 should be read in conjunction with section 18 of the Act. Under the latter provision, the sheriff is required to return all attached property or the proceeds thereof if no execution has been delivered to him within three months of the time that the order of attachment was made, or within such time as the court may order.[615]

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[612] See Part II of the Commission Report, *supra*, note 1, at 119-35.

[613] *Ibid.*, at 123-26.

[614] In the case of a writ of enforcement, see Commission Report, *supra*, note 1, Part I, ch. 3, at 124. In the case of a notice of garnishment or attachment of wages, see Commission Report, *supra*, note 1, Part II, ch. 3, at 213.

The *Small Claims Courts Act*, on the other hand, is silent insofar as the term of a warrant of attachment is concerned. It would seem, therefore, that a warrant of attachment may be enforced at any time before the disposition of the action giving rise to the attachment proceedings. Similarly, section 164 of this Act would seem to permit property taken pursuant to a warrant of attachment to be held by the bailiff until judgment in the main action has been delivered.

In the other provinces, the duration of an attachment order varies greatly. For example, the Nova Scotia Rules and the Prince Edward Island Rules provide that an attachment order may be enforced for a period of ninety days from the time of its issuance, or for such further time as the court may order.[616] By virtue of Rule 49.04(4), the expiration of this ninety day period does not affect the validity of anything done during such period. Finally, reference should be made to Rule 49.13(2). Under this Rule, if the attached property or the proceeds thereof have not been seized within sixty days of judgment and the issuance of an execution order thereunder, the sheriff must return the property.

In Manitoba, an attaching order remains in force "as long as the statement of claim is in force"[617] or, put somewhat differently, until the disposition of the main action. However, like the Ontario, Nova Scotia, and Prince Edward Island attachment legislation, Rule 611 of the Manitoba Queen's Bench Rules limits the time that attached property may remain in the sheriff's hands. On the other hand, the now repealed British Columbia *Absconding Debtors Act*[618] provided for a *prima facie* term of six months in the case of a writ of attachment, with no apparent limitation on the time that property taken under a writ of attachment could be held.

The attachment legislation in those American jurisdictions that we have examined shows a similar diversity of response to the issue of the duration of an attachment order. On the one hand, section 6211 of the

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[615] It is difficult to see how sections 5 and 18 would operate in practice. Where the sheriff has seized property belonging to the debtor shortly after the making of an order of attachment, it would seem he may hold the property for at least the three month period stipulated by section 18. However, assume that the sheriff is unable to seize any of the debtor's property for a period of three months after the granting of the order. Does section 18 prevent the sheriff from seizing any of the debtor's property after three months without court approval? Without an extension of the three month period provided for in section 18, any property seized after three months apparently would have to be returned immediately to the debtor.

[616] See r. 49.04(1) of both the Nova Scotia Rules and the Prince Edward Island Rules.

[617] Manitoba Queen's Bench Rules, *supra*, note 89, r. 587.

[618] R.S.B.C. 1960, c. 1, s. 6. The Act was repealed in 1978 by the *Attorney-General Statutes Amendment Act, 1978*, S.B.C. 1978, c. 11, s. 1.

New York Civil Practice Law and Rules provides that the debtor's property may be attached at any time before final judgment in the main action. Section 488.510 of the California Code of Civil Procedure, in comparison, states that a writ of attachment is effective for a period of three years, unless the court extends the life of the writ. Once a writ of attachment expires, property that is the subject of the writ is released from its operation.

It will be recalled that, in chapters 2 and 3 of Part II of the *Report on the Enforcement of Judgment Debts and Related Matters*, the Commission proposed that both a writ of enforcement and a notice of garnishment or attachment of wages should be effective for a period of six years and renewable.[619] Although there may be more reason to limit the term of prejudgment, as opposed to postjudgment, relief, in both cases too short a term could give rise to serious practical problems; indeed, a short term may frustrate the very purpose of the particular kind of relief. For example, in the circumstances in which prejudgment attachment would be available under the Commission's recommendations, it might not always be a simple matter to secure the debtor's property. If an attachment order were of limited duration, the efforts of the attaching creditor and the enforcement office might be wasted unless the term of the order were extended. The need to obtain extension after extension to make the remedy effective would increase substantially the cost of prejudgment relief, in addition to reducing its effectiveness: a debtor, for example, might be able to take advantage of any gap in time between extensions to dispose of his property.

It may be contended that the longer the term of an attachment order, the greater the risk to the debtor. While there is more than a grain of truth in this argument, it should be remembered that a debtor whose property is subject to attachment would not be powerless. Under the Commission's recommendations,[620] a debtor always would be able to apply for the discharge of the attachment order issued against him. In certain circumstances, he also would be free to apply to the court for modification or variation of the attachment order.

In the Commission's opinion, the most efficacious term for an attachment order would be one that is correlative with the creditor's need for security. Nevertheless, special circumstances may exist that call for either a shorter or a longer term in a particular case. Therefore, in order to serve the purpose of prejudgment attachment, but still retain flexibility, the Commission recommends that, unless the court otherwise orders, an attachment order should remain in force until final judgment is rendered in the creditor's action against the debtor. We make no recommendation regarding the length of time following judgment that attached property should be held if no writ of enforcement is delivered to the enforcement office. We do not envisage that creditors who have resorted to prejudgment attachment proceedings and who have proceeded to judgment will be less than punctilious in the filing of a writ of enforcement.

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[619] See *supra*, note 614.

[620] See *supra*, sec. 7(i)(vi).

(k) A REMEDY FOR WRONGFUL ATTACHMENT

Earlier in this chapter,[621] the Commission considered whether a person seeking prejudgment relief should be required to file a bond or undertaking for the security of a debtor whose property is sought to be attached. We there expressed our support for such a requirement, conditioned, for example, upon payment to the debtor in case he suffers damages by reason of the wrongful issue of an attachment order. In this section, we consider a related matter, that is, the extent to which an attaching creditor should be liable for damages that the debtor suffers by reason of the granting of an attachment order against him, and the manner in which the debtor should be able to assert a claim for damages for wrongful attachment. We should point out that existing absconding debtors legislation in Ontario does not deal with these matters.

In Canada, at the present time, Nova Scotia and Prince Edward Island make specific provision regarding the debtor's right to damages in the case of wrongful attachment. The rules of civil procedure in each of these jurisdictions allow a debtor "who claims that an attachment order was wrongfully granted or issued, or an attachment was wrongfully made" to ask for damages, in addition to seeking to have the attachment order set aside and his property returned.[622] It should be noted that Rule 49.10 of both the Nova Scotia Rules and the Prince Edward Island Rules gives the same right to any person "who claims an interest in any attached property".

A much more limited right to damages is available in the Province of Manitoba, and was available under the now repealed British Columbia *Absconding Debtors Act*.[623] Rule 610 of the Manitoba Queen's Bench Rules provides as follows:

> 610. Where, at any time before execution issues, it appears on motion that the defendant was not a debtor against whom an attaching order might be made under these rules at the time of the obtaining of the attaching order, the defendant shall recover his costs of defence, to be deducted from the amount of the plaintiff's claim or judgment; and the plaintiff shall be entitled to judgment or execution only for the excess, if any; and, if the taxed costs of the defendant are greater than the amount of the plaintiff's claim or judgment, the defendant shall be entitled to an order for payment of the excess forthwith.

The right of recovery under this Rule is restricted to the debtor's costs of defence.

The New York and California attachment legislation, in comparison, deals with the question of damages and the matter of legal costs. For example, since 1977, the New York Civil Practice Law and Rules has contained the following provision:

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[621] *Ibid.*, sec. 7(i)(iv).

[622] See r. 49.10(2) and (3) of both the Nova Scotia Rules and the Prince Edward Island Rules.

[623] R.S.B.C. 1960, c. 1, s. 38. The Act was repealed by the *Attorney-General Statutes Amendment Act, 1978*, S.B.C. 1978, c. 11, s. 1.

> 6212(e) The plaintiff shall be liable to the defendant for all costs and damages, including reasonable attorney's fees, which may be sustained by reason of the attachment if the defendant recovers judgment, or if it is finally decided that the plaintiff was not entitled to an attachment of the defendant's property. Plaintiff's liability shall not be limited by the amount of the undertaking.

One aspect of section 6212(e) that is worthy of note is the fact that the provision speaks of the relationship between the right to damages for wrongful attachment and the creditor's undertaking. This is a matter that is not covered by any attachment or absconding debtors legislation in Canada. The costs and damages that a debtor is entitled to claim under this section are restricted to those "which may be sustained by reason of the attachment".

The wrongful attachment provisions found in the California Code of Civil Procedure are undoubtedly the most comprehensive that we have examined.[624] "Wrongful attachment" is defined by section 490.010 of the California Code and includes the following: attachment in an action in which such relief is not authorized; attachment in an action in which the creditor does not recover judgment; and, with some exceptions, attachment of exempt property.[625] In any such case, the creditor is liable for "all damages proximately caused" and "all costs and expenses, including attorney's fees, reasonably expended in defeating the attachment",[626] but his liability will be limited to the amount of his undertaking.[627]

Section 490.030 outlines the procedure to be followed in the case of a claim for wrongful attachment. Subsection (a) of section 490.030 provides that the debtor may assert his claim "by motion made in the trial court without necessity of an independent action". The motion must be brought within one year of the final determination of the main action or the expiration of the time for appeal, whichever is later, but not before final judgment and all appeal rights have been exhausted.[628]

The California attachment legislation also deals expressly with the matter of set-off, section 490.040 of the Code of Civil Procedure providing as follows:

> 490.040. The amount of any recovery for wrongful attachment shall be offset insofar as possible against any unsatisfied amounts owed to the plaintiff by the defendant on the judgment in the action for which wrongful attachment damages are awarded.

Finally, it should be noted that the California wrongful attachment provisions, like Rule 49.10 of both the Nova Scotia Rules and the Prince Edward Island Rules, allow persons other than the debtor to recover damages for wrongful attachment "to the same extent and in the same manner as a defendant in the action".[629]

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[624] It should be noted that the California Code of Civil Procedure provides that "the right to recover for damages caused by an attachment or protective order on any common law theory of recovery" remains unaffected by the statutory right to recover damages for wrongful attachment: see West's Cal. Code Civ. Pro. (1982), §490.060.

[625] The creditor is saved from liability, under §490.010(c) of the Code, if he can show that he reasonably believed that the property attached was not exempt from attachment.

[626] West's Cal. Code Civ. Pro. (1982), §490.020(a).

[627] *Ibid.*, §490.020(b).

[628] *Ibid.*, §490.030(b).

We strongly advocate that any future Ontario attachment legislation should provide expressly for a cause of action for wrongful attachment. In our opinion, such a provision, like the bond or undertaking requirement that we have proposed should be imposed on creditors seeking prejudgment attachment, will help to deter creditor abuse of this remedy. A creditor who is made aware of the possible financial consequences of wrongful attachment is likely to weigh carefully the advantages and disadvantages of prejudgment relief, and to resort to such relief only when he is satisfied that grounds for attachment exist, and that he has a good cause of action against the debtor. An express right of action for wrongful attachment is also important from the debtor's point of view. The right to recover damages in such circumstances helps to maintain that all-important balance between the interests of the debtor and those of his creditor seeking security for a future judgment against the debtor.

While, as we have pointed out, present Ontario absconding debtors legislation does not address the question of the debtor's right to recover damages for wrongful attachment, there is a precedent for such a provision in the law of Ontario. Earlier in this chapter,[630] we referred briefly to the right of a person claiming any title to or interest in land to register a certificate of *lis pendens* or a caution against the land in question. A recent amendment to the *Judicature Act*[631] has created a cause of action for damages sustained by reason of the registration of a certificate of *lis pendens* or caution by a person without a reasonable claim to title to or interest in the land.

In the case of wrongful attachment, we see no reason to restrict the right to claim damages to debtors. In our opinion, any person claiming to be interested in property that has been attached should be able to recover damages from the attaching creditor for wrongful attachment. As we have pointed out, this is the position that has been adopted in Nova Scotia, Prince Edward Island, and California. Accordingly, we recommend that an attaching creditor should be liable to the debtor, or any person entitled to or interested in the property attached, for all damages and costs, including reasonable legal fees, sustained by reason of the wrongful issue of an attachment order, the wrongful attachment of property, or the issue of an attachment order in an action in which the creditor fails to recover judgment. The debtor's or a third person's primary source of recovery in the case of damages for wrongful attachment will, of course, be the creditor's bond or undertaking in respect of the same. The damages awarded, however, may be more or less than the amount of the bond or undertaking fixed by the court granting the order of attachment.

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[629] *Ibid.*, §490.050.

[630] See *supra*, sec. 2(a)(iii).

[631] See now R.S.O. 1980, c. 223, s. 38(4).

It will be noted that the above recommendation would not require a creditor to pay damages where he obtains judgment but the value of the property attached exceeds the amount of the judgment. While we believe that a creditor who fails to recover judgment should be liable in damages, we would not go so far as to penalize a creditor, who must satisfy the court that he has a strong *prima facie* cause of action, for achieving only partial success. In our opinion, the question is one of degree. Where the attaching creditor has failed entirely in his action, it is the Commission's view that the scales of justice ought to be tipped in the debtor's favour. Given the fact that prejudgment relief will continue to be available on an *ex parte* application, the mere fact that the creditor has been able to satisfy a court of the existence of a strong *prima facie* cause of action against the debtor should not shield him from liability. On the other hand, where a creditor has achieved partial success against the debtor, the scales of justice would seem to be more evenly balanced. Imposing liability on a creditor for damages arising from an excessive attachment in such circumstances would mean that an attaching creditor and his lawyer would have to be omniscient in order to predict with exactness the extent of the creditor's ultimate success.

Insofar as the manner of asserting a claim for damages for wrongful attachment is concerned, we note that, in the case of a claim for unreasonable registration of a certificate of *lis pendens* or caution, the *Judicature Act* now allows such a claim to be asserted in three ways.[632] First, damages may be claimed in the main action, that is, the action in which the creditor claims to be entitled to a *lis pendens*. Secondly, a separate, independent action may be commenced for that purpose. Thirdly, a claim for damages may be asserted on an application to vacate the certificate or caution.[633] However, the Civil Procedure Revision Committee, in its proposed *Judicature Act*, would abolish this third method of claiming damages for unreasonable registration of a certificate of pending litigation or a caution.[634]

In our view, a person should be free to claim damages for wrongful attachment by means of a counterclaim asserted in the main action or by way of a separate, independent action instituted for that purpose. Since a claim for damages for wrongful attachment is likely to give rise to difficult questions of liability and quantum of damages, we do not believe that any purpose would be served if we were to recommend a motion for the recovery of damages, as is now possible under the California attachment legislation. Therefore, the Commission recommends that a debtor's claim for damages for wrongful attachment should be asserted by way of counterclaim in the action giving rise to the attachment order, or by way of a separate, independent action. While we envisage that, in most cases, a counterclaim will be the most convenient and economical method to seek damages for wrongful attachment, there may well be circumstances in which a counterclaim will not be practical. Moreover, in the case of a claim for damages by a person other than the debtor, it will be impossible to proceed by way of counterclaim.

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[632] See s. 38(5) of the *Judicature Act*, *supra*, note 27.

[633] *Ibid.*, s. 39(1) and (3).

[634] See Williston Committee Revised Judicature Act, *supra*, note 26, s. 50(5).

The final matter with which we wish to deal in this section is the question of set-off. Assume that the attaching creditor does recover judgment against the debtor, but that the attachment order was issued wrongfully, and the debtor is successful in his claim for damages for wrongful attachment. We believe that it would be unfair to treat the judgments as being entirely independent of one another. To ensure that justice is done, and in order to avoid costly and unnecessary duplication of enforcement activity, we recommend that the amount of any recovery for wrongful attachment should be offset insofar as possible against any unsatisfied amounts owed to the attaching creditor by the debtor on the judgment in the main action.

(l) A CURATIVE PROVISION

At the beginning of this chapter,[635] the Commission pointed out that the courts, in construing legislation governing prejudgment relief, have adopted a strict constructionist approach. This demand for strict compliance with all statutory requirements has, in our view, greatly weakened the prejudgment remedies of attachment and garnishment. We believe that the safeguards that we have proposed are such that it should no longer be necessary to put form over substance in this area of the law.

To guarantee that substantive justice is done where a creditor applies for an attachment order, a number of jurisdictions have included in their attachment legislation a curative provision. Rule 49.12(a) of the Nova Scotia and Prince Edward Island Rules, for example, authorizes a court to grant a creditor "a reasonable opportunity to amend any affidavit or bond used in support of the grant of an attachment order". Section 6223 of the New York Civil Practice Law and Rules allows a court, on a motion to vacate or modify an order of attachment, to give the attaching creditor "a reasonable opportunity to correct any defect". The Commission believes that a similar provision should be included in any future Ontario attachment legislation. Consequently, we recommend that, both before and after an attachment order issues, a court should be expressly empowered to allow all amendments necessary to secure the advancement of justice, upon proper terms as to costs and otherwise.[636]

RECOMMENDATIONS

The Commission makes the following recommendations:

1. (1) Except in the family law context, a creditor should be able to look only to his debtor's property for provisional relief. Accordingly, the provisions of the *Fraudulent Debtors Arrest Act* concerned with prejudgment arrest should be repealed.

   (2) Section 24 of the *Family Law Reform Act*, insofar as it authorizes

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[635] See *supra*, secs. 2(b)(i) and (ii).

[636] This proposal is similar in terms to r. 185 of the Ontario Rules of Practice, *supra*, note 15. For the proposals of the Civil Procedure Revision Committee, see Williston Committee Rules, *supra*, note 26, rr. 1.03 and 2.02.

prejudgment arrest, should be retained. However, the section should be amended to require the debtor to be brought before the court as soon as possible after his arrest to show cause why he should not be detained. At this time, the onus should be on the creditor to satisfy the court that the debtor is guilty of the conduct alleged. Failure to so satisfy the court should result in the debtor's immediate release.

2. With the exception of section 22 of the *Family Law Reform Act*, existing provisional remedies should be repealed and replaced by a new prejudgment remedy – to be called "attachment" – the details of which are contained in the following Recommendations. Accordingly, the *Absconding Debtors Act* and the absconding debtors provisions of the *Small Claims Courts Act* should be repealed. In addition, *Mareva* injunctions should no longer be available under section 19(1) of the *Judicature Act*. The only authority for the courts to restrain debtors from dealing with their assets prior to judgment to the detriment of their creditors should be the new prejudgment attachment legislation proposed below.

3. Prejudgment attachment should be available only in the following circumstances:

   (a) where a debtor is about to leave or has left Ontario with intent to defeat, defraud, hinder, or delay his creditors or any of them, or to avoid being served with civil process;

   (b) where the debtor conceals himself to avoid service of civil process;

   (c) where a debtor has removed or is about to remove his property from the Province, or has assigned, transferred, disposed of, encumbered or secreted his property, or is about to assign, transfer, dispose of, encumber or secrete his property, with intent to defeat, defraud, hinder, or delay any of his creditors, or where the debtor has done or omitted to do any act with respect to his property with intent to frustrate the enforcement of a judgment that might be rendered against him; or

   (d) whenever there is a danger that, without such relief, recovery of a debt may be jeopardized.

4. Prejudgment attachment should not be available only because

   (a) the debtor is about to leave or has left the jurisdiction with intent to avoid arrest or to change his domicile;

   (b) the debt or liability of the debtor is alleged to have been fraudulently incurred; or

   (c) the debtor is not a resident of Ontario.

5. Unlike the case under the *Absconding Debtors Act*, prejudgment attachment should be available whether or not the debtor is an Ontario resident.

6. Prejudgment attachment should be available irrespective of the nature of the creditor's underlying claim, and should not be restricted to contract claims or claims sounding in debt.

7. Prejudgment attachment should be available regardless of the amount claimed in a creditor's action against the debtor.

8. Prejudgment attachment should be available only in those cases where Ontario courts would have jurisdiction *in personam* over the defendant pursuant to the principles at common law or under Rule 25 of the Supreme Court of Ontario Rules of Practice. The mere fact that there are grounds for prejudgment relief should not be sufficient to permit an Ontario court to claim jurisdiction over a dispute.

9. Prejudgment attachment should be available irrespective of whether the creditor has commenced an action against the debtor and, where such relief is granted before the commencement of an action, the court should be empowered to fix such terms and conditions respecting the commencement of an action against the debtor as to it seem just.

10. Subject to Recommendation 11, all of a debtor's property, real and personal, debts included, should be subject to prejudgment attachment.

11. Subject to Recommendation 12, all debtors subject to prejudgment attachment should be able to claim the postjudgment enforcement exemptions proposed in Parts I, II, and III of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*, irrespective of the grounds for attachment.

12. A debtor's wages, salary, and other similar income should be exempt entirely from prejudgment attachment.

13. Subject to Recommendation 16, in order to create a system of prejudgment attachment that will properly balance the interests of debtors and creditors, and to give maximum flexibility, there should be a broad jurisdiction to order any method or methods of attachment considered just and equitable, having regard to all the circumstances of the case, including the type of property sought to be attached and the desirability of avoiding hardship to the parties or any interested person. In particular, it should be possible to order "attachment" by physical seizure, notional seizure (or "walking possession"), registration of the order under the *Personal Property Security Act*, or by way of an injunction.

14. Where physical seizure or "walking possession" is ordered, it should be effected in the same manner as postjudgment seizure, and the

Commission's proposals respecting the postjudgment seizure of a debtor's personal property should apply equally to prejudgment seizure of such property.

15. (1) In order to enable prejudgment attachment to be effected by means of registration of an attachment order under the *Personal Property Security Act*, the Act should be amended to accommodate such registration.

    (2) The attaching creditor should be under a duty to have the registration of an attachment order deleted if he is no longer entitled to the attachment order (for example, where the creditor has been paid or where the attachment order has been discharged or dissolved). Failure to do so should result in the creditor's liability for any damages that the debtor may suffer as a result.

16. In the case of realty, prejudgment attachment should be required to be effected by the registration of a copy of the attachment order against the title of the debtor's property pursuant to the terms of the *Registry Act* or the *Land Titles Act*, which should be amended to accommodate the registration of such orders.

17. In order to protect debtors, prejudgment attachment should be available only after the creditor has established under oath the existence of one or more grounds for attachment and a strong *prima facie* case on the claim against the debtor, and has affirmed the amount that he seeks to recover from the debtor over and above all set-offs and counterclaims known to him, and that his application for prejudgment attachment is made *bona fide* for the sole purpose of obtaining security for the enforcement of any future judgment in the main action against the debtor.

18. The jurisdiction to grant prejudgment attachment should be exercised by a judge.

19. (1) Prejudgment attachment should continue to be available upon an *ex parte* application. To provide the debtor with additional protection in such a case, however, the order should be granted for a limited period of time and the attaching creditor should be required to return to court to seek a continuation of the attachment order. On a return of the motion, the onus should continue to rest upon the attaching creditor to satisfy the court that there are grounds for prejudgment attachment.

    (2) In order to enable the debtor to meet the creditor's claim for a continuation of an attachment order or to challenge the validity of the order, he should be served with a copy of the order together with a copy of the material supporting the creditor's original application.

20. (1) In order to safeguard further the interests of the debtor and persons interested in property subject to prejudgment attachment, the issuance of an attachment order should be dependent upon the

creditor posting a bond or giving an undertaking in an amount, to be determined by the court, that will cover the plaintiff's probable liability for wrongful attachment (see Recommendations 29-31).

(2) As a precondition to the making of an attachment order, the attaching creditor should also be required to undertake to pay the costs incurred by a third party as a result of the order of attachment.

21. The court should be empowered to order the release of any attached property and its restoration to the debtor or to any person entitled thereto upon the receipt of substitute security that, in the court's opinion, is adequate. The right to substitute other property for the attached property should be available irrespective of the method or methods of attachment employed.

22. Legislation governing prejudgment attachment should contain an express provision empowering the debtor or any other person claiming to be interested in attached property to apply, in accordance with the rules of civil procedure, for the dissolution of the attachment order.

23. (1) The court should have a broad power to vary, modify, or discharge an attachment order in the following circumstances: (a) where the creditor has failed to proceed with his action against the debtor with reasonable diligence; (b) where the creditor's action has been discontinued, dismissed, or compromised; (c) where the amount of the creditor's claim has been either reduced or increased; or (d) where other just cause exists. Property affected by such an order should be restored in accordance with the terms of the order of the court.

(2) Any person claiming to be interested in attached property should be able to apply for the variation, modification, or discharge of an attachment order.

24. The proposals in chapter 5 of Part II of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters* regarding the resolution of disputes respecting the ownership of property that arise in the course of postjudgment enforcement proceedings should apply *mutatis mutandis* to the resolution of such disputes in the prejudgment attachment context.

25. (1) The court, upon the application of the debtor, the creditor, the enforcement office, or any person interested in the attached property, and upon notice to all concerned, should be empowered to order the sale or disposition of any attached property where it is likely to perish or depreciate materially in value before the probable termination of the creditor's action against the debtor, or where the keeping of the property is likely to result in unreasonable loss or expense, or for any other just cause.

(2) The court should determine the manner and the terms of any sale, having regard to, *inter alia*, the nature of the attached property and the method of attachment employed.

(3) The costs incurred in a sale or disposition of attached property should be a first charge against the proceeds realized.

26. Where the value of any attached property would be diminished substantially as a result of any delay in its sale in accordance with Recommendation 25, the enforcement office should be authorized to take any reasonable steps necessary to preserve the value of the property, including its sale in the manner recommended for expeditious sale of property in the postjudgment enforcement context. The costs incurred to preserve the value of the property should be a first charge on the property or the proceeds realized on a sale thereof.

27. In order to enable those interested in the sale of attached property to avoid the costs of an application for sale pursuant to Recommendation 25, the creditor, the debtor whose property has been attached, and any other interested person should be able to consent to the sale by the enforcement office, without court approval, of any attached property before judgment has been handed down in the main action.

28. In order to serve the security purpose of prejudgment attachment but still retain flexibility, an attachment order should remain in force until final judgment is rendered in the creditor's action against the debtor, unless the court otherwise orders.

29. The attaching creditor should be liable to the debtor, or any person entitled to or interested in the property attached, for all damages and costs, including reasonable legal fees, sustained by reason of the wrongful issue of an attachment order, the wrongful attachment of property, or the issue of an attachment order in an action in which the creditor fails to recover judgment. No liability should attach where the creditor obtaining prejudgment relief recovers a judgment against the debtor, even if the value of the property attached exceeds the amount of the creditor's judgment.

30. A claim for wrongful attachment should be asserted either by way of a counterclaim in the action giving rise to the attachment order or by means of a separate, independent action.

31. The amount recovered in an action for wrongful attachment should be offset insofar as possible against any unsatisfied amounts owed to the attaching creditor by the debtor as a result of judgment in the main action.

32. Legislation governing prejudgment attachment should contain a curative provision, expressly empowering the court to allow all amendments necessary to secure the advancement of justice, upon proper terms as to costs and otherwise.

CHAPTER 3

VOIDABLE TRANSACTIONS

1. GENERAL INTRODUCTION

(a) SCOPE OF THE CHAPTER

In this chapter, consideration will be given to the circumstances in which a transaction between a debtor and another party may be set aside on the basis that it constitutes a fraud on creditors of that debtor. Conceptually, and for the purposes of this chapter, a distinction may be drawn between a fraudulent conveyance[1] and a fraudulent or unjust preference.[2] A fraudulent conveyance is a transfer by the debtor of his property to a third party other than a creditor, whereas a fraudulent preference is a payment by the debtor to one or more, but not all, of his creditors, the transferee or transferees being preferred thereby. While the language of the *Fraudulent Conveyances Act*[3] would seem to comprehend both fraudulent conveyances and fraudulent preferences, the orthodox view is that the Act is restricted to the voiding of fraudulent conveyances.[4]

In considering fraudulent conveyances and preferences, an attempt will be made to provide a coherent picture of provincial legislation and the voluminous case law that supplements it. In fact, it is a measure of the inadequacy of the legislation that the case law is of such critical importance in providing flesh for the very skeletal statutory framework.

In addition to considering the jurisprudence in Ontario, the law in other jurisdictions will be canvassed. As a general proposition, it may be said that there is a fair degree of similarity in provincial legislation and case law across Canada. All provinces cxcept Newfoundland have legislation dealing with fraudulent preferences, and separate legislation dealing with fraudulent conveyances has been adopted in British Columbia, Manitoba, Quebec, and Newfoundland. In the other provinces, pre-*Law of Property Act 1925*[5] English fraudulent conveyance legislation[6] remains in force as part of the general law. Finally, all common law provinces except Newfoundland have a separate fraudulent conveyance provision appearing in statutes devoted mainly to fraudulent preferences.

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[1] "Conveyance" is defined in s. 1(*a*) of the *Fraudulent Conveyances Act*, R.S.O. 1980, c. 176.

[2] The term "preference" is not defined in the *Assignments and Preferences Act*, R.S.O. 1980, c. 33. The term "unjust preference" is used in s. 4(2) of the *Assignments and Preferences Act*, but the term "fraudulent preference" is the more popular and will be used in this chapter.

[3] *Supra*, note 1.

[4] See *infra*, this ch., sec. 3(b). However, there would appear to be several instances in which a conveyance to a creditor (that is, a preference) has been successfully challenged under both the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act*.

Reference will also be made to the provisions of the *Bankruptcy Act*,[7] the proposed new bankruptcy legislation,[8] section 172 of the English *Law of Property Act 1925*, and the American Uniform Fraudulent Conveyance Act.[9] A consideration of these statutes, as well as proposals for reform in New Brunswick, will provide several possible models for reform in Ontario.

(b) LEGISLATIVE HISTORY

The original precursors of the Ontario *Fraudulent Conveyances Act* are two statutes of Elizabeth I. The first, 13 Eliz., c. 5, generally has its counterpart in sections 2, 3, and 4 of the *Fraudulent Conveyances Act*,[10] dealing with conveyances that are fraudulent against creditors. The second, 27 Eliz., c. 4, dealt with conveyances in fraud of purchasers and is reflected in sections 5, 6, 7, and 8 of the *Fraudulent Conveyances Act*, to which no further reference will be made.

Both statutes of Elizabeth were consolidated in the 1897 Revised Statutes of Ontario.[11] In addition, reference should be made to *The Voluntary Conveyances Act* of 1868,[12] which effected an amendment to 27 Eliz., c. 4, insofar as the latter Act was in force in Ontario.[13] The 1868 Act appeared as sections 11-13 of *The Law of Property Amendment Act* in the 1877 Revised Statutes[14] and again in 1887 as *The Voluntary and Fraudulent*

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[5] *Law of Property Act 1925*, c. 20 (U.K.).

[6] 13 Eliz., c. 5 (1571).

[7] R.S.C. 1970, c. B-3.

[8] *Bankruptcy Act, 1980*, Bill C-12, 1980 (32d Parl. 1st Sess.) (hereinafter referred to as "Bill C-12").

[9] National Conference of Commissioners on Uniform State Laws, Uniform Fraudulent Conveyance Act, Uniform Laws Ann. (1978), Vol. 7A. This Act was approved in 1918 by the National Conference of Commissioners on Uniform State Laws and the American Bar Association. Twenty-five states have adopted the Uniform Act.

[10] The penal provisions of 13 Eliz., c. 5, have been omitted from the Ontario statute. In England, s. 172 of the *Law of Property Act 1925* has replaced, with amendments, 13 Eliz., c. 5. There has been some controversy as to whether s. 172 is only a clarification of the earlier statute or whether it introduces some new elements. Section 172 consolidated the *Law of Property (Amendment) Act 1924*, which significantly altered 13 Eliz., c. 5. See *Lloyds Bank Ltd. v. Marcan*, [1973] 1 W.L.R. 339, at 344, [1973] 2 All E.R. 359, at 367, aff'd [1973] 1 W.L.R. 1387, [1973] 3 All E.R. 754 (C.A.) (subsequent references are to [1973] 2 All E.R.).

[11] R.S.O. 1897, c. 334.

[12] 31 Vict., c. 9.

[13] See, now, *Fraudulent Conveyances Act*, *supra*, note 1, s. 8.

[14] R.S.O. 1877, c. 95.

Conveyances Act.[15] The latter appeared unamended in the 1897 Revised Statutes.[16] In 1911, both 13 Eliz., c. 5, as consolidated, and the 1868 Act, as consolidated, were themselves consolidated and re-enacted as *The Fraudulent Conveyances Act*.[17] The statute has remained essentially unamended since that time.

The *Assignments and Preferences Act* first appeared consolidated as sections 17 and 18 of *The Indigent Debtor's Act*.[18] These provisions were continued in the 1877 Revised Statutes.[19] Section 2 of the latter Act was superseded in 1885.[20] The 1885 statute, along with section 1 of chapter 118 of the 1877 Revised Statutes,[21] were consolidated with amendments in the 1887 Revised Statutes.[22] In 1910, the Act was re-enacted in amended form[23] and, subject to minor amendments, has appeared in the same form to the present time.

2. FRAUDULENT CONVEYANCES

(a) THE LEGISLATIVE FRAMEWORK

Notwithstanding the existence of 13 Eliz., c. 5, and its Ontario counterpart dealing with fraudulent conveyances, the precursors of the *Assignments and Preferences Act* also attempted to invalidate fraudulent conveyances. However, there has been no real suggestion that the enactment of these later provisions has repealed by implication the *Fraudulent Conveyances Act*.[24]

Sections 1 to 4 of the *Fraudulent Conveyances Act*, the main piece of legislation dealing with fraudulent conveyances, provide as follows:

> 1. In this Act,
>
> (*a*) 'conveyance' includes gift, grant, alienation, bargain, charge, encumbrance, limitation of use or uses of, in, to or out of real property or personal property by writing or otherwise;

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[15] R.S.O. 1887, c. 96.

[16] R.S.O. 1897, c. 115.

[17] 1 Geo. 5, c. 24.

[18] C.S.U.C. 1859, c. 26.

[19] *An Act respecting the Fraudulent Preference of Creditors by persons in insolvent circumstances*, R.S.O. 1877, c. 118, ss. 1 and 2.

[20] *An Act respecting Assignments for the Benefit of Creditors*, 48 Vict., c. 26.

[21] See *supra*, note 19.

[22] *An Act respecting Assignments and Preferences by Insolvent Persons*, R.S.O. 1887, c. 124.

[23] *The Assignments and Preferences Act*, 10 Edw. 7, c. 64.

[24] See *Bank of Montreal v. Crowell* (1980), 37 N.S.R. (2d) 292, 67 A.P.R. 292 (S.C., T.D.), at 301, *per* Hallett J. Hallett J. based his conclusion that the Nova Scotia equivalents of the two Ontario Acts could co-exist on the ground that, under 13 Eliz., c. 5, a creditor in Nova Scotia could attack a conveyance made by a solvent person, an action impossible under the *Assignments and Preferences Act*, R.S.N.S. 1967, c. 16. See, also, *infra*, note 42 and supporting text. But see *Federal Business Development Bank v. Van Klaveren* (1979), 25 N.B.R. (2d) 79, 51 A.P.R. 79 (S.C., T.D.), at 84, *per* Barry J., by way of *obiter dictum*.

> (*b*) 'personal property' includes goods, chattels, effects, bills, bonds, notes and securities, and shares, dividends, premiums and bonuses in a bank, company or corporation, and any interest therein;
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> (*c*) 'real property' includes lands, tenements, hereditaments and any estate or interest therein.
>
> 2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns.
>
> 3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and *bona fide* to a person not having at the time of the conveyance to him notice or knowledge of the intent set forth in that section.
>
> 4. Section 2 applies to every conveyance executed with the intent set forth in that section notwithstanding that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of *bona fides* and want of notice or knowledge on the part of the purchaser.

The relevant provisions of the *Assignments and Preferences Act* dealing with fraudulent conveyances are contained in sections 4(1), 5(1), and 12:[25]

> 4.-(1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full, or knows that he is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice his creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced.
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> 5.-(1) Nothing in section 4 applies . . . to any *bona fide* sale . . . made in the ordinary course of trade or calling to an innocent purchaser . . . nor to any *bona fide* conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in consideration of a present actual *bona fide* payment in money, or by way of security for a present actual *bona fide* advance of money, or that is made in consideration of a present actual *bona fide* sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor.
>
> 12.-(1) In the case of a gift, conveyance, assignment or transfer of any property, real or personal, that is invalid against creditors, if the person to

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[25] Some of the provisions in ss. 4 and 5 deal solely with fraudulent preferences and assignments for the general benefit of creditors. Such assignments are not discussed in this Report.

whom the gift, conveyance, assignment or transfer was made has sold or disposed of, realized or collected the property or any part thereof, the money or other proceeds may be seized or recovered in an action by a person who would be entitled to seize and recover the property if it had remained in the possession or control of the debtor or of the person to whom the gift, conveyance, transfer, delivery or payment was made, and such right to seize and recover belongs not only to an assignee for the general benefit of the creditors of the debtor but, where there is no such assignment, to all creditors of the debtor.

(2) Where there is no assignment for the benefit of creditors and the proceeds are of such a character as to be seizable under execution, they may be seized under the execution of any creditor and are subject to the *Creditors' Relief Act*.

(3) Where there is no assignment for the benefit of creditors and the proceeds are or are not of such a character as to be seizable under execution, an action may be brought therefor by a creditor, whether an execution creditor or not, on behalf of himself and all other creditors, or such other proceedings may be taken as are necessary to render the proceeds available for the general benefit of the creditors.

(4) This section does not apply as against innocent purchasers of the property.[26]

(b) THE PRESENT LAW

While the purpose and practical effect of the two provincial statutes coincide or overlap in many respects, there are areas in which, largely for historical reasons, the two diverge. It is proposed to deal with fraudulent conveyances under the two Acts from a topical perspective. The pertinent statutory provisions and case law will be considered in respect of such matters as jurisdictional factors, proof and use of presumptions, the role of consideration, protected transactions, persons having standing to impugn transactions, and the following of proceeds.

(i) Void or Voidable?

Although both section 2 of the *Fraudulent Conveyances Act* and section 4(1) of the *Assignments and Preferences Act* use the term "void" in respect of a transaction affected by the legislation, it has always been held that the transaction is only voidable; that is, the transaction is good as between the parties until successfully impeached by a creditor.[27]

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[26] Although s. 12 appears in the *Assignments and Preferences Act*, it has been held that the proceeds of a conveyance declared invalid under the *Fraudulent Conveyances Act* also can be followed pursuant to s. 12: see *Westinghouse Canada Ltd. v. Buchar* (1975), 9 O.R. (2d) 137, 59 D.L.R. (3d) 641, 20 C.B.R. (N.S.) 246 (C.A.) (subsequent reference is to 9 O.R. (2d)), overruling *Gray v. Quinn* (1922), 22 O.W.N. 325 (H.C. Div.).

[27] *Donohoe v. Hull Brothers & Co.* (1895), 24 S.C.R. 683. In this connection, reference should be made to the present English equivalent of the Ontario provisions. Section 172(1) of the *Law of Property Act 1925*, *supra*, note 5, provides, *inter alia*, that a fraudulent conveyance "shall be voidable" against persons prejudiced by it.

(ii) The Financial Status of the Debtor

Unlike under the *Fraudulent Conveyances Act*, section 4(1) of the *Assignments and Preferences Act* provides that, in order to invoke the provisions of that Act, a creditor first must prove that, at the time of the disposition of the property, the debtor was "in insolvent circumstances or [was] unable to pay his debts in full, or [knew] that he [was] on the eve of insolvency".[28] The definition of "insolvency" usually cited is that given by Rose J. in *Rae v. McDonald*:[29] legal insolvency occurs where the debtor has not sufficient exigible property to pay all his debts if sold under legal process, while commercial insolvency is the inability to discharge one's financial obligations as they become due. Either definition would appear to satisfy the jurisdictional requirements of section 4(1). Although the wording is somewhat ambiguous, the phrase "unable to pay his debts in full" appears to refer to legal insolvency, while "insolvent circumstances" could refer to either legal or commercial insolvency.[30]

There is also some confusion concerning how a debtor's financial status is to be calculated. More particularly, it is not clear whether future assets and liabilities must form part of the equation. A recent New Brunswick Report[31] concluded that, "[a]t most . . . it would appear that only future obligations which are liquidated in amount and not subject to any contingency may be included in the determination of whether a debtor is solvent".[32] However, reference should be made to the Nova Scotia case of *Traders Group Ltd. v. Mason*,[33] in which Gillis J. held that a guarantee, even though a contingent liability, is a liability for the purpose of a proceeding under 13 Eliz., c. 5.[34] In many cases, of course, the existence of contingent liabilities will be such as to alert the debtor that "he is on the eve of insolvency".[35]

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[28] See *Carmody v. Amorde* (1930), 38 O.W.N. 62 (C.A.). See, also, *supra*, note 24.

[29] *Rae v. McDonald* (1887), 13 O.R. 35 (C.A.).

[30] See New Brunswick Department of Justice, Law Reform Division, *Third Report of the Consumer Protection Project*, Vol. II, *Legal Remedies of the Unsecured Creditor After Judgment* (1976) (hereinafter referred to as "New Brunswick Report"), at 108.

[31] *Ibid.*

[32] *Ibid.*, at 109, *n*. 121. The Report cited *Bertrand v. Canadian Rubber Co.* (1897), 12 Man. R. 27 (Q.B.) as an example of a case where the possible inclusion of future assets and liabilities in the determination of insolvency was contemplated. However, the Report concluded that, since a creditor with an unliquidated claim was not a creditor within the meaning of the *Assignments and Preferences Act*, R.S.N.B. 1973, c. A-16 (see *Ashley v. Brown* (1890), 17 O.A.R. 500), it was not likely that his claim would be included in the determination of insolvency. Since proof of insolvency is not a prerequisite to bringing an action under 13 Eliz., c. 5 (in force in New Brunswick), the Report did not comment on the determination of insolvency in respect of such an action. However, as we shall see, the majority of actions taken under the Ontario *Fraudulent Conveyances Act* involve legally or commercially insolvent debtors, since debtors who are solvent and who remain solvent upon a conveyance by definition still possess the financial wherewithal to pay their debts.

In connection with the exclusion of a future unliquidated or uncertain claim, see s. 4(*a*) of Bill C-12, *supra*, note 8:

> 4. For the purposes of this Act, a person is insolvent where
>
> (*a*) the property of the person, if it were realized at a fair value, would be insufficient to pay all his certain and liquidated debts whether or not the debts are due; . . .

[33] *Traders Group Ltd. v. Mason* (1973), 43 D.L.R. (3d) 76 (N.S.S.C., T.D.), varied (1974), 53 D.L.R. (3d) 103 (N.S.S.C., App. Div.) (subsequent reference is to 43 D.L.R. (3d)).

A further ambiguity concerns whether the value of the debtor's assets taken at the time of the impeached transaction should be their market value or their value at a forced sale. The majority of commentators and judges appear to favour an execution sale valuation,[36] although others have expressed contrary, or at least skeptical, views.[37]

There does seem to be agreement, however, that non-exigible assets cannot be included in assessing whether a debtor is solvent or insolvent.[38] Moreover, a transaction involving exempt property cannot be impugned under either provincial statute, since ordinarily the disposition of such property cannot have the effect of delaying, hindering, defeating, or defrauding creditors.[39]

Finally, as the New Brunswick Report stated, "[i]t appears that unwillingness to pay, as opposed to inability to pay, does not constitute insolvency".[40] The Report, however, did note some controversy in respect of this issue.[41]

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[34] *Ibid.*, at 90. In *Halsbury's Laws of England* (4th ed., 1977), Vol. 18, at 172-73, para. 367, it is stated that, "[i]n determining the amount of the transferor's indebtedness, account must be taken of any contingent liability, such as that under a guarantee, or for damages recovered in an action begun after the conveyance for a tort committed prior to the conveyance, unless the contingency of the transferor being made liable is very remote . . ." (footnotes omitted). See, also, *Union Bank v. Tyson* (1915), 7 W.W.R. 1117 (B.C.S.C., T.D.), and *In re Ridler, Ridler v. Ridler* (1882), 22 Ch. D. 74.

[35] See *Assignments and Preferences Act*, *supra*, note 2, s. 4(1).

[36] See *Rae v. McDonald*, *supra*, note 29, *per* Cameron C.J.; Scane, "Fraudulent Conveyances" (1964), 3 Western Ont. L. Rev. 40, at 42, citing *Re Butterworth* (1882), 19 Ch. D. 588; *Davidson v. Douglas* (1868), 15 Gr. 347; and *Dominion Bank v. Cowan* (1887), 14 O.R. 465 (C.P. Div.).

[37] See *Rae v. McDonald*, *supra*, note 29, *per* Rose J. See, also, s. 4(*a*) of Bill C-12, *supra*, note 8, quoted *supra*, note 32, and *Bankruptcy Act*, *supra*, note 7, s. 2(*c*), which defines an "insolvent person" to include, *inter alia*, a person "the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due".

[38] See Scane, *supra*, note 36, at 42. See, also, *McGuire v. The Ottawa Wine Vaults Co.* (1913), 48 S.C.R. 44, at 54, 13 D.L.R. 81, and Hurley, "Transfers for Insufficient Consideration in Oregon" (1957), 36 Ore. L. Rev. 313, at 317.

[39] See *Lodor v. Creighton* (1860), 9 U.C.C.P. 295, and *Salter v. WYO-BEN Products Inc.* (1972), 25 D.L.R. (3d) 626 (Alta. S.C., T.D.). See, also, Dunlop, *Creditor-Debtor Law in Canada* (1981), at 341-45, esp. at 345, *n*. 54.

[40] New Brunswick Report, *supra*, note 30, at 110, citing *McLean v. Ratekin*, 22 Sask. L.R. 633, [1928] 4 D.L.R. 18, [1928] 2 W.W.R. 421, 10 C.B.R. 156 (C.A.).

[41] New Brunswick Report, *supra*, note 30, at 111, *n*. 124. In this connection, reference should be made to the provisions of Bill C-12, *supra*, note 8. Section 4(*b*) provides as follows:

> 4. For the purposes of this Act, a person is insolvent where . . .
>
> (*b*) the person has ceased to pay his certain and liquidated debts generally as they become due.

It bears repeating that section 4(1) of the *Assignments and Preferences Act* requires, as a jurisdictional matter, proof of insolvency, inability to pay debts in full, or knowledge of impending insolvency, whereas, under the *Fraudulent Conveyances Act*, there is no such jurisdictional requirement. But, despite the absence of an express reference to insolvency, the state of the debtor's finances is obviously of critical importance under the latter statute. Creditors ordinarily will not seek to impugn a transaction by a debtor who was solvent at the time of the transaction or who was not rendered insolvent thereby.[42] The conveyance of property while insolvent is clearly formidable evidence of fraudulent intent; indeed, creditors may use the debtor's insolvency to raise a presumption of fraud.[43] In practice, the majority of fraudulent conveyance cases involve insolvent debtors conveying property for nominal or no consideration. The implications of this important fact will be discussed at a later juncture; suffice it to state here that the absence of a formal insolvency requirement under the *Fraudulent Conveyances Act* should not mask the practical realities of being forced to prove fraudulent intent essentially by determining the embarrassed state of the debtor's finances when the transaction was effected.

(iii) Proving the Fraudulent Intent of the Debtor: Presumptions and Inferences

The *sine qua non* of both provincial statutes is what we may call, for convenience, the debtor's "fraudulent" intent *vis-à-vis* his creditors. While the *Assignments and Preferences Act* uses the term "prejudice", whereas the *Fraudulent Conveyances Act* uses the term "defraud", there seems to be no real difference with respect to the type of intent required to be shown; the word "defraud" is not used in a technical, legal sense, and the term "fraud" or "fraudulent intent" commonly is used in actions pursuant to either statute.

With respect to the invocation of either Act, attention invariably

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The provision does not appear to be restricted to mere inability to pay. Moreover, s. 5(3)(*b*) provides:

> 5.-(3) A person is deemed, unless the contrary is proved, to have ceased to pay his certain and liquidated debts generally as they become due where, within ninety days prior to the filing of a petition or a proposed arrangement . . .
>
> (*b*) he stops making payments in the ordinary course of business.

The present *Bankruptcy Act* distinguishes between inability to pay and stoppage of payment. The definition of "insolvent person" in s. 2 includes, *inter alia*, a person

> (*a*) who is for any reason unable to meet his obligations as they generally become due, or
>
> (*b*) who has ceased paying his current obligations in the ordinary course of business as they generally become due.

[42] But see *Bank of Montreal v. Crowell*, *supra*, note 24, at 301, where Hallett J. stated that, if 13 Eliz., c. 5, were not in force in Nova Scotia, "there would be an unsatisfactory gap in our law as solvent persons who made fraudulent conveyances would otherwise appear to be immune from attack". However, it would appear that, in order to succeed, the impeaching creditor would have to show that the solvent debtor rendered himself insolvent by the conveyance (see *ibid.*, at 302 *et seq.*). See, also, *supra*, note 24 and supporting text.

[43] See *infra*, this ch., sec. 2(b)(iii).

focuses on the difficult problems ostensibly faced in proving the debtor's intent. At first blush, the contention that the apparent subjectivity or amorphous nature of the concept is a substantial impediment appears reasonably based: who can deny the difficulties of probing the real intentions and motives of individuals, particularly where concealment and subterfuge are cleverly used to camouflage the real nature and purpose of the transaction? Yet, an analysis of the case law goes some considerable distance to belie the above contention. The courts have declared on innumerable occasions that the validity or invalidity of a transaction must be determined objectively, having regard to the actions of the parties and the debtor's financial position at the time of the transaction.[44] The courts have been more than willing to raise presumptions and draw inferences of fraudulent intent from all the surrounding circumstances. The important presumption that one intends the natural consequences of one's actions has been used to impute fraudulent intent where no direct proof has been forthcoming. In fact, the instances in which direct proof of such intent has been found are very few indeed. As mentioned earlier, in most cases an insolvent debtor has conveyed property for nominal or no consideration: the natural effect of the transaction has been such as to raise what in practice is an almost irrebuttable presumption of fraudulent intent. Accordingly, it is arguable that the critical issues concern the consideration given and the debtor's financial status, rather than his true intentions or motives. While satisfactory proof of a debtor's financial status is by no means a simple task, at least it may be determined objectively.

a. *"Badges of Fraud"*

Several indicia, or badges, of fraud have been legitimized by the case law. The presence of these badges of fraud has been said to give rise to an inference of fraudulent intent. The following badges are the most common:[45] (1) the retention of some benefit by the debtor, such as his continuance in possession of the conveyed property, unless such possession is consistent with the nature and purpose of the transaction, as in the case of a mortgage; (2) the fact that the conveyance includes substantially all the debtor's assets; (3) secrecy; and (4) the fact that an action is pending or that an execution has been issued.

Ferguson v. Lastewka[46] illustrates the effect of the presence of several badges of fraud. In that case, the debtor was serving a jail term as a result of a car accident in respect of which a civil action was expected. In these circumstances, he conveyed his farm property, his major asset, to his son-in-law. However, subsequent to the conveyance and after serving his sentence, the debtor returned to the farm and he and his wife continued to live there for some time. Despite the presence of valuable consideration, the Court held that an intent to defraud had been sufficiently proved. The existence of a badge of fraud, although not conclusive, shifted the onus from the plaintiff to the defendant.[47]

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[44] For example, in *Bank of Montreal v. Crowell*, *supra*, note 24, Hallett J. quoted from the opinion of Harrison J. in *McGillan v. McGillan*, [1947] 4 D.L.R. 456 (N.B.S.C., App. Div.), at 460, as follows: "The court is not interested in [the debtor's] mental processes, but in his intentions as evidenced by his actions."

[45] See, for example, *Bank of Montreal v. Vandine*, [1953] 1 D.L.R. 456, 33 M.P.R. 368 (N.B.S.C., App. Div.) (subsequent reference is to [1953] 1 D.L.R.); *Kapicki v. Andriuk*, [1975] 2 W.W.R. 332 (Alta. Dist. Ct.); *Ferguson v. Lastewka*, [1946] O.R. 577, [1946] O.W.N. 685, [1946] 4 D.L.R. 531 (H.C.J.) (subsequent references are to [1946] O.R.); and *Twyne's Case* (1602), 3 Co. Rep. 80b, 76 E.R. 809 (Star Chamber).

[46] *Supra*, note 45.

The shifting of the burden of proof also occurs where a debtor conveys property to a close relative. The nature of the onus of proving fraudulent intent where relatives are involved was touched upon in *Owen Sound General and Marine Hospital v. Mann*.[48] In that case, Anger J. stated that "[t]he burden of proving fraudulent intent by the parties to a conveyance is ordinarily upon the plaintiff, but nevertheless where there is a conveyance between near relatives which has the effect of defeating or delaying creditors, although there is no absolute rule that the burden of proof is upon the defendants, the principle of *res ipsa loquitur* may properly be applied to a transaction between near relatives in suspicious circumstances, so as to place upon the defendants the burden of establishing by corroborative evidence other than the testimony of interested parties, the *bona fides* of the transaction . . .".[49]

Many other cases illustrate how presumptions and inferences of fraudulent intent have served to weaken the notion that the court's main concern is to uncover the debtor's subjective motives or intent in conveying his property.

b. Presumptions and the Natural Consequences of the Transaction

As indicated above, the courts have been quick to come to the aid of those seeking to impugn a transaction by an insolvent debtor where the transaction involved nominal or no consideration.[50] We now turn to the jurisprudence concerning what in some cases has been called an irrebuttable presumption of fraudulent intent, dependent entirely on the effect of the transaction. It should be stated at the outset that, in the main, the case law affirming this presumption represents earlier jurisprudence. As we shall see, most of the more modern authorities have rejected the existence of an irrebuttable presumption, but have endorsed a rebuttable presumption as the more orthodox interpretation of 13 Eliz., c. 5, and its descendants.

The central principle in this area is the presumption that one intends the natural consequences of one's actions,[51] as determined by all the circumstances of the case. Having regard to this presumption, one line of cases has held that, where the effect of the conveyance was to defraud creditors – for example, where an insolvent debtor made a voluntary, that is, gratuitous, conveyance – the intent to defraud must be presumed. In the landmark decision of *Freeman v. Pope*,[52] Lord Chancellor Hatherley stated the rule as follows: "[I]f the necessary effect of the instrument was to defeat, hinder, or delay the creditors, that necessary effect was to be considered as evidencing an intention to do so".[53] This rule, which seemed to become more rigid in the subsequent cases relying upon *Freeman v. Pope*, was applied to avoid "speculating as to what was actually passing in the mind of the settlor, which can hardly ever be satisfactorily ascertained . . .".[54]

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[47] See *Halsbury's Laws of England* (4th ed., 1977), Vol. 18, at 171, para. 365.

[48] *Owen Sound General and Marine Hospital v. Mann*, [1953] O.R. 643, [1953] 3 D.L.R. 417 (H.C.J.) (subsequent reference is to [1953] O.R.).

[49] *Ibid.*, at 647. Anger J. cited the important case of *Koop v. Smith* (1915), 51 S.C.R. 554, 25 D.L.R. 355.

[50] Where there is consideration, it has been stated that an actual intent to defeat creditors must be proved: see *Hickerson v. Parrington* (1891), 18 O.A.R. 635. However, even here, courts may have regard to any of the badges of fraud to which reference already has been made. By this means, courts have managed to assist plaintiffs who lack concrete evidence of actual fraudulent intent. They have also managed, however, to create confusing and conflicting jurisprudence, often emasculating completely the notion of fraudulent intent.

While the principle that the necessary effect of the conveyance must govern did not originate with *Freeman v. Pope*,[55] this case is by far the most widely known and widely cited. In many of the earlier cases, and in some later cases, courts expressly sought to refute the notion that proof of actual fraudulent intent was required where the effect of the transaction was to defeat creditors. For example, in *Jeffrey v. Aagaard*,[56] an insolvent debtor made a gratuitous settlement of all his property on his wife. In the Court of Appeal, Cameron J.A. endorsed the trial judge's view[57] that, "although no fraudulent intent was . . . established, the effect of the conveyance was to bring them within the statute 13 Eliz."[58] In Ontario, Mowat V.C. stated in *Irwin v. Freeman*[59] that, "[t]his debt, then, being due at the time the impeached deed was executed, *Spirett v. Willows*[60] is an express authority that the deed of gift is void as against the plaintiff, whether it was fraudulent in actual intention or not; and it is unnecessary to consider further whether there was intentional fraud or not in giving the deed".

Freeman v. Pope, or the rule with which that case is associated, continues in more modern times to be cited and followed, albeit sporadically.[61] However, as a manifestation of the uncertainty of the law in this area, a parallel line of cases has rejected this rule. In some instances, courts have converted the rule into what is tantamount to a rebuttable presumption. For example, in *Elgin Loan and Savings Co. v. Orchard*,[62] Britton J. stated that, "*[i]n the absence of any direct proof of intention*, if the necessary effect is that some of the creditors would remain unpaid, the intent to defeat, hinder, or delay must be inferred".[63] In other instances, courts have made it clear that the necessary effect of the transaction is not the sole determining factor.

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[51] See *Freeman v. Pope* (1870), L.R. 5 Ch. App. 538; *McGillan v. McGillan*, *supra*, note 44; *Wood v. Irwin* (1869), 16 Gr. 398, at 402-03; and *Crawford v. Meldrum* (1866), 3 E. & A. 101, at 117.

[52] *Supra*, note 51.

[53] *Ibid.*, at 540.

[54] *Ibid.*

[55] See, for example, *Skarf v. Soulby* (1849), 1 Mac. & G. 364, at 375, 41 E.R. 1306 (Ch.), and *Smith v. Cherrill* (1867), L.R. 4 Eq. 390, at 395.

[56] *Jeffrey v. Aagaard*, [1922] 2 W.W.R. 1201 (Man. C.A.). See, also, *Bludoff v. Osachoff* (1928), 22 Sask. L.R. 533, [1928] 3 D.L.R. 179, [1928] 2 W.W.R. 150 (C.A.).

[57] The trial judge cited *Mackay v. Douglas*, (1872), L.R. 14 Eq. 106, 41 L.J. Ch. 539, 26 L.T. 721, 20 W.R. 652 (subsequent reference is to L.R. 14 Eq.), followed in *The Ottawa Wine Vaults Co. v. McGuire* (1912), 8 D.L.R. 229, 27 O.L.R. 319 (App.Div.), aff'd (1913), 48 S.C.R. 44, 13 D.L.R. 81; *Buckland v. Rose* (1859), 7 Gr. 440; *Ware v. Gardner* (1869), L.R. 7 Eq. 317, 38 L.J. Ch. 348; and *Sun Life Assurance Co. of Canada v. Elliott* (1900), 31 S.C.R. 91.

[58] *Jeffrey v. Aagaard*, *supra*, note 56, at 1202.

[59] (1867), 13 Gr. 465, at 473-74.

[60] (1865), 3 DeG.J. & S. 293, 46 E.R. 649 (Ch.).

Given the language of 13 Eliz., c. 5, and of the *Fraudulent Conveyances Act*, it is not surprising that the jurisprudential pendulum has swung away from the strict rule represented by *Freeman v. Pope*. The case most associated with the now more orthodox doctrine – that the effect of the transaction is not conclusive and that a transaction will be valid if there is no intent to defraud, whatever its effect – is *Re Wise, Ex parte Mercer*.[64] In that case, a conveyance without consideration was made by a debtor in the face of pending litigation against him. Lord Esher M.R. dismissed as "monstrous"[65] the view that, as a matter of law, a conveyance must be characterized as having been made with the intent to defraud in all cases where its necessary effect was to defeat or delay creditors. While the court must take into account the effect of the transaction in determining the debtor's intent, the court also must consider all the other circumstances of the case. Lord Esher M.R.'s synopsis of the implications of the hitherto received dogma contained a trenchant criticism of *Freeman v. Pope*:[66]

> But, if other circumstances make you believe that the man did not intend to do that which you are asked to find that he did intend, to say that, because that was the necessary result of what he did, you must find, contrary to the other evidence, that he did actually intend to do it, is to ask one to find that to be a fact which one really believes to be untrue in fact.

The rejection of the strict *Freeman v. Pope* rule in Ontario began even prior to *Freeman v. Pope*,[67] and has continued, although not unabatedly. In *Hickerson v. Parrington*,[68] Osler J.A. concluded that "[i]t is not enough to prove that the result of the deed is to delay or exclude creditors". In *Bank of Montreal v. Stair*,[69] Rose J., after noting the "very many broad statements" in such cases as *Freeman v. Pope*, quoted Meredith J.A. in *The Ottawa Wine Vaults Co. v. McGuire*,[70] who stated that "rules, based on certain circumstances, as to when a transaction should be, and when it should not be, considered fraudulent, must always give way if they conflict with the very truth regarding the question of intent".[71] In *Mandryk v. Merko*,[72] Freedman J.A. agreed that the broad language used in *Freeman v. Pope* was comprehensive enough to warrant the construction normally given to it, but he stated that it was not intended to be applied in every case. In support of this view, he quoted with approval the judgment of Lord Esher M.R. in *Re Wise, Ex parte Mercer*.[73] With respect to the troublesome language of Sedgewick J. in *Sun Life Assurance Co. of Canada v. Elliott*[74] – who stated that, where the effect of the transaction is prejudicial, the transaction is void, "no matter what the intent of the settlor was" – Freedman J.A. noted that, in that case, the debtor clearly had a fraudulent intent, so that the quoted phrase ought to be regarded as *obiter*.

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[61] See, for example, *Rimco Ltd. v. Leon Developments Ltd.* (1971), 4 N.S.R. (2d) 592 (S.C., T.D.); *Traders Group Ltd. v. Mason*, *supra*, note 33, following *Sun Life Assurance Co. of Canada v. Elliott*, *supra*, note 57; and *Bank of Montreal v. Crowell*, *supra*, note 24, citing the above three cases, as well as *Freeman v. Pope*, *supra*, note 51. The *Sun Life* decision was applied in *Atlantic Acceptance Corp. v. Distributors Acceptance Corp.*, [1963] 2 O.R. 18, 38 D.L.R. (2d) 307 (H.C.J.). See, also, Scane, *supra*, note 36.

[62] *Elgin Loan and Savings Co. v. Orchard* (1904), 7 O.L.R. 695 (H.C.J.).

[63] *Ibid.*, at 698 (emphasis in original).

[64] *Re Wise, Ex parte Mercer* (1886), 17 Q.B.D. 290 (C.A.).

[65] *Ibid.*, at 298.

[66] *Ibid.*, at 298-99.

[67] See, for example, *Buckland v. Rose*, *supra*, note 57, at 442.

[68] *Supra*, note 50, at 642.

[69] *Bank of Montreal v. Stair* (1918), 44 O.L.R. 79, 46 D.L.R. 718 (H.C.J.) (subsequent reference is to 44 O.L.R.).

It is not possible here to attempt to reconcile the approaches in *Freeman* and *Mercer*.[75] Suffice it to state that the issue as to the correct test is of substantial significance in both theory and practice.

(iv) Protected Transactions under the *Fraudulent Conveyances Act*

Sections 3 and 4 of the *Fraudulent Conveyances Act* protect certain transactions from being set aside under section 2. We now turn to consider the rather unsatisfactory state of the law relating to these saving provisions.

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[70] *Supra*, note 57.

[71] The quote appears *supra*, note 69, at 82-83. See, also, *Owen Sound General and Marine Hospital v. Mann*, *supra*, note 48, and *Carr v. Corfield* (1890), 20 O.R. 218 (H.C.J.).

[72] [1971] 19 D.L.R. (3d) 238, 2 W.W.R. 542, 15 C.B.R. (N.S.) 246 (Man. C.A.). *Mandryk v. Merko* has been followed, for example, in *Henry Electric Ltd. v. White*, [1976] W.W.D. 10 (B.C.S.C.).

[73] See quotation of Lord Esher M.R. in text supporting note 66, *supra*.

[74] *Supra*, note 57, at 94-95.

[75] However, a brief observation may be made at this juncture. In *Re Wise, Ex parte Mercer*, *supra*, note 64, at 300, Lord Esher M.R. stated that "it was not the necessary consequence of what [the debtor] did to defeat or delay the plaintiff . . .". The Court refused to discuss the effect of 13 Eliz., c. 5, in such a case. In light of this fact, one commentator has stated that, "[i]f, therefore, *Ex p. Mercer, re Wise* is taken to decide only that intent to defraud must be proved as a fact *except in cases where the inevitable result of making a settlement is to defeat or delay creditors*, it is possible to reconcile the dicta": Langstaff, "The Cheat's Charter?" (1975), 91 L.Q. Rev. 86, at 95-96 (emphasis added). (This approach was taken in *Carruthers v. Peake* (1911), 55 S.J. 291 (Ch.), *per* Warrington J.). Langstaff then concluded (at 99) that fraudulent intent "may not only be established as a matter of fact where direct evidence shows that the grantor had that actual intent, but also as a matter of law where the necessary effect of a conveyance is to defeat or delay creditors". Whether this rationalization deals satisfactorily with the case where the effect is to defeat creditors, but where at the same time there is also direct evidence indicating the absence of a fraudulent intent, is a troubling point. In this connection, see the quotation of Lord Esher M.R. in text supporting note 66, *supra*.

a. "Bona Fide" Conveyances

To what does the term "*bona fide*" in section 3 of the *Fraudulent Conveyances Act* refer? Does it characterize the state of mind of the debtor? Does the term refer to the transferee? Or does the term simply mean that the transaction must be a genuine transaction and not a sham?[76]

While each of the interpretations noted above has its proponents, it appears to be more generally assumed that the term "*bona fide*" is used subjectively and must refer either to the debtor or to his transferee.[77] Grammatically, it is not unreasonable to suppose that the debtor's good faith, among other factors, is required to save a transaction. However, since section 3 of the *Fraudulent Conveyances Act* is invoked only where the debtor has the intent set forth in section 2, at first blush it is difficult to adopt this construction. How can the debtor have, at the same time, "the intent set forth" in section 2 and be *bona fide*? If fraudulent intent and *bona fides* are diametrically opposed, then section 3 would never save a transaction, since it would be impossible to prove the fraudulent debtor to be *bona fides*.

Others have claimed that "*bona fide*" must refer to the state of mind of the transferee.[78] However, this interpretation of section 3 is still not free from difficulties. First, the construction somewhat strains the language of the section. Secondly, what is the relationship between the transferee's good faith and his want of notice or knowledge of the debtor's fraudulent intent? In this connection, it has been said that "it seems impossible to imagine that bad faith can exist independently of notice of an intent to defraud creditors".[79] Accordingly, under such an interpretation, *bona fides* would seem to be redundant.[80]

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[76] See *Banque d'Hochelaga v. Potvin*, [1924] 1 D.L.R. 678, at 681, [1924] 1 W.W.R. 488, at 491-92 (Alta. S.C., App. Div.), where it was stated that the transaction must be "on the whole, fair and honorable" and not a "sham". See, also, *Re Moroney*, 21 L.R. Ir. Ch. 27 (C.A.), at 54, where Porter M.R. spoke in terms of the "reality" of the transaction. Curran J. spoke in similar terms and cited *Re Moroney*, in *Union Bank of Canada v. Murdock* (1917), 34 D.L.R. 150, [1917] 2 W.W.R. 112 (Man. K.B.), rev'd on other grounds (1917), 37 D.L.R. 522, [1917] 3 W.W.R. 820 (Man. C.A.).

In the New Brunswick Report, *supra*, note 30, at 125-26, the presence of badges of fraud was said to bespeak a lack of *bona fides*. See, also, Thompson, "Fraudulent Conveyances – Remedies of Creditors and Purchasers – Attachment" (1954), 30 N.D.L. Rev. 99, at 100-01, and *Re Panfab Corp. Ltd., Duro Lam Ltd. v. Last*, [1971] 2 O.R. 202, (1970), 17 D.L.R. (3d) 382 (H.C.J.).

[77] See *Halsbury's Laws of England* (4th ed., 1977), Vol. 18, at 176, para. 375; Langstaff, *supra*, note 75, at 89-90; and a criticism of Langstaff in Elkan, "Voluntary Conveyances to Defraud Creditors" (1975), 91 L.Q. Rev. 317.

[78] See Scane, *supra*, note 36, at 46. Some statutes have even codified this view. Section 60(3) of the New Zealand *Property Law Act 1952*, 1952, No. 51, comparable to Ontario section 3, provides that s. 60 "does not extend to any estate or interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intention to defraud creditors". Of this provision, one commentator has said:

> 'Good faith' presumably means that he takes without knowledge of the fact that the alienation may be a fraud on the creditors of the alienor. But this conclusion seems so surprising that further examination is needed.

Cain, "Consideration and the Fraudulent Conveyance" (1960), 36 N.Z.L.J. 251.

[79] Langstaff, *supra*, note 75, at 90. In *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, at

A third interpretation of the term "*bona fide*" appears in the New Brunswick Report, where it is said that "[t]he requirement that protected transactions must be in good faith seems interpreted to mean that there must be a genuine transfer of the real interest in the property involved in the transaction from the debtor to his grantee".[81] Whatever the accuracy of this statement in New Brunswick, where 13 Eliz., c. 5, remains in force, it raises some difficulties under the Ontario *Fraudulent Conveyances Act*. In this connection, reference should be made to section 4 of that Act, which reads as follows:

> 4. Section 2 applies to every conveyance executed with the intent set forth in that section notwithstanding that it was executed upon a valuable consideration *and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred*, unless it is protected under section 3 by reason of *bona fides* and want of notice or knowledge on the part of the purchaser. [Emphasis added.]

Under section 4, *bona fides* appears to be clearly differentiated from a genuine transfer "to and for the benefit of the transferee [of] the interest expressed to be thereby transferred".

In practice, courts have all but ignored the ambiguity surrounding the term "*bona fide*". The more critical need to investigate the intent of the debtor and, as we shall see, the intent of the transferee,[82] has virtually stilled attempts at statutory interpretation.

b. The Role of Consideration

(1) *"Good" and "Valuable" Consideration*

It will be recalled that the term "good consideration" is used in section 3, and "valuable consideration" in section 4 of the *Fraudulent Convey-*

529, Sedgewick J. stated that "knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith . . .". However, if "*bona fide*" and the transferee's "notice or knowledge" of the debtor's intent can be read separately, that assertion is of little relevance: under this approach, even if the transferee has acted *bona fide*, the transaction would fall because of the transferee's "notice or knowledge".

[80] In view of the dilemma, one commentator considered the possibility that the want of notice requirement in s. 172(3) of the U.K. *Law of Property Act 1925*, *supra*, note 5, akin to s. 3 of the *Fraudulent Conveyances Act*, was introduced simply out of an abundance of caution "to ensure that if bad faith were judicially taken to mean participation in a fraud on creditors, and not mere knowledge of it, the section would still give effective protection to creditors": Langstaff, *supra*, note 75, at 90. However, he did not find this interpretation convincing, and rightly so. Any transferee participating in the debtor's attempted fraud obviously must have "notice of the [debtor's] intent to defraud creditors" under s. 172(3) of the *Law of Property Act 1925*. Notice or knowledge of the fraud is the more comprehensive of the two requirements and, accordingly, would include "participation in a fraud on creditors".

[81] New Brunswick Report, *supra*, note 30, at 125.

[82] See *infra*, this ch., secs. 2(b)(v)a.(2) and 2(b)(iv)c.

ances Act. In the United Kingdom, section 173(3) of the *Law of Property Act 1925* provides that section 172(2), akin to section 2 of the Ontario Act, "does not extend to any estate or interest in property conveyed for valuable consideration and in good faith or upon good consideration and in good faith to any person not having, at the time of the conveyance, notice of the intent to defraud creditors". The phrase "good consideration" is used in 13 Eliz., c. 5, but the statute did not mention valuable consideration. However, at the time of the enactment of that statute, the two expressions were apparently regarded as synonymous.[83]

It should be made clear that full consideration is not essential to uphold a conveyance under the *Fraudulent Conveyances Act*.[84] However, while the courts do not weigh the adequacy of consideration "in too nice scales",[85] nominal or grossly inadequate consideration[86] is not sufficient.[87] The real problem, however, is the interpretation to be given to "good consideration" and "valuable consideration". While some courts use the terms interchangeably, and some ignore the existence of the two terms in the same statute,[88] others have expressed dissatisfaction with these approaches.[89] Moreover, controversy exists respecting whether "good consideration" comprehends "natural love and affection". One commentator has suggested that this interpretation would give the term "good consideration" its "ordinary meaning", although he conceded that, since in 13 Eliz., c. 5, the term "may have meant what is now meant by 'valuable consideration'",[90] natural love and affection would not satisfy the real intent of 13 Eliz., c. 5.[91]

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[83] In *Union Bank of Canada v. Murdock*, *supra*, note 76, Curran J., commenting on 13 Eliz., c. 5, used the expression "good (i.e. valuable) consideration". See, also, *Cromwell v. Comeau* (1957), 8 D.L.R. (2d) 676, 39 M.P.R. 347 (N.S.S.C.) (subsequent references are to 8 D.L.R. (2d)), *per* Doull, J. In *Lloyds Bank Ltd. v. Marcan*, *supra*, note 10, at 368, it was said that "the expression 'good consideration' clearly comprises alike valuable and non-valuable consideration". In *Bank of Montreal v. Crowell*, *supra*, note 24, at 303, Hallett J., also commenting on 13 Eliz., s. 5, said: "The consideration must be 'good consideration'; so-called meritorious consideration, that is, love and affection, is not valuable consideration *and therefore not consideration within the meaning of the Statute of Elizabeth*" (emphasis added).

[84] See *Leighton v. Muir* (1962), 34 D.L.R. (2d) 332 (N.S.S.C.); *Reaume v. Guichard* (1856), 6 U.C.C.P. 170; *Carradice v. Currie* (1872), 19 Gr. 108; *Owen Sound General and Marine Hospital v. Mann*, *supra*, note 48; *Stephens v. Olive* (1786), 2 Bro. C.C. 90, 29 E.R. 52 (Ch.); *Nunn v. Wilsmore* (1800), 8 Term. Rep. 521, 101 E.R. 1524 (K.B.); *Copis v. Middleton* (1818), 2 Madd. 410, 56 E.R. 386 (C.A.); and *Thompson v. Webster* (1859), 4 DeG. & J. 600 (Ch.), aff'd (1861), 4 L.T. 750 (H.L.).

[85] *Buckland v. Rose*, *supra*, note 57, at 448.

[86] See *Fleming v. Edwards* (1896), 23 O.A.R. 718. In the Divisional Court, Armour C.J. stated (at 722) that the consideration in question "was a grossly inadequate consideration, and as such was a badge of fraud . . .". In *Hickerson v. Parrington*, *supra*, note 50, at 643, Osler J.A. stated that "there is no clear and sufficient proof that the consideration was inadequate". Another example of a decision in which a judge seemed to require "adequate" consideration was that of McDermid J.A. in *Toronto-Dominion Bank v. Michael* (1972), 32 D.L.R. (3d) 498, at 502, [1973] 1 W.W.R. 656, at 660-61 (Alta. S.C., App. Div.). "Very inadequate" consideration can indicate suspicious circumstances: *Bank of Montreal v. Vandine*, *supra*, note 45.

[87] *Meeker Cedar Products Ltd. v. Edge* (1968), 68 D.L.R. (2d) 294, 12 C.B.R. (N.S.) 49, aff'd (1968), 1 D.L.R. (3d) 240, 12 C.B.R. (N.S.) 60 (S.C.C.).

[88] See, for example, *Re Eichholz*, [1959] Ch. 708, [1959] 2 W.L.R. 200, *per* Harman J.

[89] See Langstaff, *supra*, note 75, at 86 *et seq.*, and the critique in Elkan, *supra*, note 77, at 319-20.

[90] *Lewin on Trusts* (16th ed., 1964), at 112.

Before canvassing the relationship between consideration and the transferee's intent, brief mention should be made of the rationale for section 4 of the *Fraudulent Conveyances Act* – a section that, despite the wide interpretation given to "good consideration" in 13 Eliz., c. 5, uses the term "valuable consideration" and introduces the notion of a genuine transfer of property. This "curious provision"[92] appears to be a reaction to the English case of *Wood v. Dixie*,[93] where the Court of Queen's Bench rejected the trial judge's jury direction to the effect that, even where there was valuable consideration and a genuine intention to transfer the property, the transfer was void if made to defeat creditors. *Wood v. Dixie* was criticized,[94] but followed,[95] in Ontario until 1872, when the precursor of section 4 was enacted, presumably to overrule the case.[96]

(2) *Consideration and the Transferee's "Notice or Knowledge"*

There is a close relationship between consideration and the necessity to prove "notice or knowledge" on the part of the transferee. It is clear law that, where the conveyance is voluntary or is without good consideration, the person impeaching the conveyance need show only the intent of the debtor to defraud his creditors; the transferee's notice or knowledge of the debtor's intent is irrelevant.[97]

However, where either good or valuable consideration is given, the complainant must prove an intent on the part of the debtor to defraud his creditors and that the transferee had "notice or knowledge" of that intent.[98] These are indeed formidable obstacles for an impeaching creditor. In *Harman v. Richards*,[99] for example, it was said that "those who undertake to impeach for *mala fides* a deed which has been executed for valuable consideration have . . . a task of great difficulty to discharge".[100] In *Cameron v. Cusack*,[101] Osler J.A. quoted[102] the language of Fry J. in *In re Johnson, Golden v. Gillam*[103] to the effect that "the fact that there is valuable consideration shews at once that there may be purposes in the transaction other than the defeating or delaying of creditors, and renders the case, therefore, of those who contest the deed more difficult". While intent may be inferred from the necessary effect of the conveyance and from the so-called "badges of fraud", if a transferee for consideration is ignorant of the debtor's actual or imputed fraudulent intent, the conveyance stands.[104]

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[91] See *Cromwell v. Comeau*, *supra*, note 83, *per* Doull J. See, also, *Bank of Montreal v. Crowell*, *supra*, note 24. Concerning the proposition that "good consideration" cannot mean natural love and affection, since this interpretation would nullify the purpose of the Act, see *Dutton v. Poole* (1678), 2 Lev. 210, 89 E.R. 523 (K.B.); *Cadogan v. Kennett* (1776), 2 Cowp. 432, 98 E.R. 1171 (K.B.) (subsequent reference is to 98 E.R.); and *Corlett v. Radcliffe* (1860), 14 Moo. P.C. 121, 15 E.R. 251.

[92] See Dunlop, *supra*, note 39, at 523.

[93] (1845), 7 Q.B. 892, 115 E.R. 724.

[94] See, for example, *White v. Stevens* (1850), 7 U.C.Q.B. 340.

[95] See, for example, *Smith v. Moffatt* (1869), 28 U.C.Q.B. 486.

[96] 35 Vict., c. 11, s. 1.

[97] See *Oliver v. McLaughlin* (1893), 24 O.R. 41 (Q.B. Div.); *Gauthier v. Woollatt*, [1940] 1 D.L.R. 275 (Ont. H.C.J.); *Union Bank of Canada v. Murdock*, *supra*, note 76; *Davies v. Dandy* (1920), 54 D.L.R. 134, [1934] 2 W.W.R. 126 (Man. C.A.); *Banque d'Hochelaga v. Potvin*, *supra*, note 76; *Cromwell v. Comeau*, *supra*, note 83; and *Traders Group Ltd. v. Mason*, *supra*, note 33.

[98] *Hickerson v. Parrington*, *supra*, note 50; *Ferguson v. Lastewka*, *supra*, note 45; *Cadogan v. Kennett*, *supra*, note 91; and *Bank of Montreal v. Crowell*, *supra*, note 24. See, also, the cases cited *supra*, note 97. It appears that the burden of proof is on the transferee to prove the existence of good or valuable consideration: *Banque d'Hochelaga v. Potvin*, *supra*, note 76.

[99] (1852), 10 Hare 81, 68 E.R. 847 (V.C.) (subsequent reference is to 68 E.R.).

(3) *Full Consideration*

Before leaving the issue of consideration, brief mention should be made of the situation where full consideration is given for a conveyance. To convey more fully the ostensible purpose of the existing law of voidable transactions, reference ought to be made to judicial opinions that appear to ignore the consequences of giving full consideration. Concentrating on the fraudulent design of the transaction, and not on its ultimate effect, Lord Mansfield stated in *Cadogan v. Kennett*:[105]

> But if the transaction be not bona fide, the circumstance of its being done for a valuable consideration, will not alone take it out of the statute. I have known several cases where persons have given a fair and full price for goods, and where the possession was actually changed; yet being done for the purpose of defeating creditors, the transaction has been held fraudulent, and therefore void.
>
> One case was, where there had been a decree in the Court of Chancery, and a sequestration. A person with knowledge of the decree, bought the house and goods belonging to the defendant, and gave a full price for them. The Court said, the purpose being with a manifest view to defeat the creditor, was fraudulent, and therefore, notwithstanding a valuable consideration, void . . . .[106]

On the other hand, in the United States, one commentator has summarized the general position by stating that even an insolvent person could transfer property validly "if sufficient consideration were received".[107] He said further that, "[i]f there is a corresponding increase in the debtor's assets, the creditors are not prejudiced, because they are in no worse position than they were before the conveyance".[108] Yet, he continued in the following manner:[109]

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[100] *Ibid.*, at 851.

[101] *Cameron v. Cusack* (1890), 17 O.A.R. 489.

[102] *Ibid.*, at 494.

[103] *In re Johnson, Golden v. Gillam* (1881), 20 Ch. D. 389, at 392.

[104] See *McDonald v. Horan* (1908), 12 O.W.R. 1151 (H.C.J.), and *Perras v. Brault*, [1940] S.C.R. 547.

[105] *Supra*, note 91, at 1172. The language of Lord Mansfield was quoted by Spragge V.C. in *Smith v. Moffatt*, *supra*, note 95, at 496. See, also, *McMullen v. Dr. Barnardo's Homes National Incorporated Association* (1924), 26 O.W.N. 168 (App. Div.), where the conveyance was avoided notwithstanding that full consideration was given. Orde J.A. was of the view that the giving of the consideration was itself part of a fraudulent scheme to defeat the creditor.

[106] See, also, Mack, "Fraudulent Conveyances – Now and Hereafter" (1980), 32 C.B.R. (N.S.) 82, at 89, where it was said that s. 2 of the *Fraudulent Conveyances Act* "indeed is not limited solely to voluntary conveyances but will also affect conveyances where full consideration is exchanged if the transaction is entered into with knowledge by both parties of intent to prejudice creditors of one of them".

> If the insolvent owns property worth $100 and sells it to another for $100, *in the absence of a fraudulent intent on the part of the grantee*, the creditors will not be heard to complain. In such a case the creditor is in no worse position than he was before the conveyance.

On its face, the above argument seems somewhat strange indeed: a conveyance to a non-fraudulent grantee giving $100 for property worth $100 cannot prejudice creditors, whereas a conveyance to a fraudulent grantee giving $100 for property worth $100 does prejudice creditors. The importance of the grantee's intent or motive to the ultimate position of the creditors is by no means self-evident. It may well be possible that some forms of consideration given to a debtor may place creditors in a worse position *vis-à-vis* the debtor than if the property itself were retained, even if the consideration is fair and reasonable relative to the value of the property. However, it is not likely that this refinement was considered in arriving at the conclusion that a transaction may be impeached even where the full price was paid. Rather, the focus has been on fraudulent intent – the foundation of existing voidable transactions law – notwithstanding that, all other things being equal, the necessary effect of the conveyances in question would not prejudice the creditors.

c. *The Transferee's "Notice or Knowledge" of the Debtor's Fraudulent Intent*

Given the emphasis in the statute and case law on the debtor's fraudulent intent, it is not at all surprising that, in order to save a transaction, the transferee must not have any notice or knowledge of such intent. As we have said, however, the issue concerning the presence or absence of such notice or knowledge can arise only where a conveyance is made with either good or valuable consideration; if the conveyance is voluntary, an impeaching creditor need prove only the fraudulent intent of the debtor.

Notwithstanding that the *Fraudulent Conveyances Act* uses the phrase "notice or knowledge" of the debtor's fraudulent intent, this requirement has come to be known as the "concurrent intent doctrine", and it is not uncommon for judges and commentators to state that the transferee somehow must be more intimately connected with the debtor's fraud. Indeed, it has been suggested that an impeaching creditor must prove that the transferee himself had a fraudulent intent.

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[107] Hurley, *supra*, note 38, at 317, citing *Kane v. Sesac, Inc.*, 54 F. Supp. 853 (S.D.N.Y. 1944).

[108] Hurley, *supra*, note 38, at 317.

[109] *Ibid.*, at 325 (emphasis added).

Unfortunately, the language used in the cases makes it difficult to state a categorical rule in this area. For example, in *Hickerson v. Parrington*,[110] Osler J.A. said that "[t]he case, therefore, is one of that class in which in order to defeat the deed there must be proof of an actual and express intent to defraud creditors, and the purchaser must be shewn to have been privy to such intent . . .".[111]

It is not clear from the cases whether the term "privy", or other similar terms, is meant to imply some type of direct or indirect participation in the debtor's scheme, although the language of the statute would seem to belie such an interpretation.[112] Such terms seem active rather than passive in respect of the transferee's connection with the debtor's fraudulent scheme. In *Lloyds Bank Ltd. v. Marcan*,[113] Pennycuick V.-C. stated:[114]

> In *Re Fasey*[115] . . . P.O. Lawrence, J., made it clear that what is required is simply that the transferee shall not have notice of the intent to defraud. It is not sufficient to enable him to take advantage of the section to show that he was not actually implicated in the fraudulent intention.

Pennycuick V.-C. also stated that "[n]otice must, I think, plainly include constructive notice".[116] Presumably, constructive notice may be found where the circumstances surrounding the transaction should have led the transferee to inquire as to the *bona fides* of the transaction or the intention of the debtor. "Knowledge", on the other hand, would appear to mean actual knowledge; it is difficult to imagine constructive knowledge.

But, even if "notice" comprehends constructive notice, one apparently cannot take the matter too far. For example, where a conveyance is for value, notice of the debtor's insolvency is not *per se* notice of his fraudulent intent.[117] Moreover, it has been held in Ontario that knowledge of the prejudicial effect of a conveyance is not sufficient. In *Crawford v. Meldrum*,[118] Spragge V.C. said that, even if the transferee "knew that the effect of her purchase would be to disappoint some of the creditors, unless that was her motive for making the purchase, it will not be a reason for avoiding it".[119] While it may be argued that the knowledge referred to by Spragge V.C. ought not to be sufficient, it seems questionable that creditors must prove that the transferee's "motive" was to "disappoint some of the creditors". Again, the statute does not appear to go this far.

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[110] *Supra*, note 50.

[111] *Ibid.*, at 640-41. The use of the term "express" is somewhat novel and surprising. Osler J.A. cited *Re Johnson, Golden v. Gillam*, *supra*, note 103, and *Middleton v. Pollock* (1876), 2 Ch. D. 104 (C.A.). See, also, *Bank of Montreal v. Vandine*, *supra*, note 45, and Scane, *supra*, note 36, at 46, citing *Hickerson v. Parrington*, *supra*, note 50, *Ferguson v. Lastewka*, *supra*, note 45, and *Owen Sound General and Marine Hospital v. Mann*, *supra*, note 48.

[112] The editor of *Halsbury's Laws of England* appears to resist the contention that some form of participation is required to be shown, stating that "[t]he statutory exception is not available where, at the time of the conveyance to him, a transferee had notice of the transferor's intent to defraud, even though the transferee was not himself implicated in the fraud": *Halsbury's Laws of England* (4th ed., 1977), Vol. 18, at 176, para. 376. Section 172(3) of the *Law of Property Act 1925*, *supra*, note 5, requires the absence of "notice of the intent to defraud creditors". However, reference should be made to an earlier statement in *Halsbury's Laws of England* (at 169, para. 362) that "[i]t is ordinarily not necessary to show that the transferee was actually implicated in the transferor's fraudulent intention save insofar as may be necessary in the case of a conveyance for valuable consideration".

[113] *Supra*, note 10.

[114] *Ibid.*, at 369. (The quotation in the Weekly Law Reports erroneously refers to s. 5, rather than s. 6, of 13 Eliz., c. 5.)

[115] [1923] 2 Ch. 1.

[116] *Lloyds Bank v. Marcan*, *supra*, note 10, at 369.

[117] *Mulcahy v. Archibald*, *supra*, note 79.

Before leaving this issue, reference should be made to the analysis contained in the New Brunswick Report.[120] The Report did not accept the express language of 13 Eliz., c. 5, at its face value. It stated that "[m]ere knowledge of the debtor's intent on the part of the person who has given consideration will not make the transaction voidable . . . although the actual words of the English statute indicate that notice of the improper intent may be fatal to the rights of a third party".[121] After citing cases to support this proposition, the Report continued as follows:[122]

> There need be no conflict between this position and the wording of section 6 of the English statute. In setting aside the transaction made by the debtor, the issue is the intent of the transaction. Under the existing jurisprudence, if the third party gives valuable consideration, there must be concurrence of intent to attack the transaction. Mere knowledge of the debtor's improper intent does not create a concurrence of intent.

Finally, after stating that the "test . . . is whether [the transferee] is privy to the fraud against creditors",[123] the Report offered these comments concerning privity:[124]

> Privity would undoubtedly exist if the third party shared the actual intent to defeat creditors . . . . If the third party's own intent is to gain a good bargain for himself, some form of collusion or assistance with the deliberate object of helping the debtor to carry out his improper intent would probably be necessary.

By way of conclusion, then, it may be said that, notwithstanding the apparently clear language of section 3 respecting the transferee's "notice or knowledge", there seems to be no unanimity regarding the precise meaning to be given to these terms. The absence of a universally accepted rule is, of course, of no little significance in an area of the law already characterized by a considerable degree of ambiguity.

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[118] *Supra*, note 51.

[119] *Ibid.*, at 107.

[120] New Brunswick Report, *supra*, note 30.

[121] *Ibid.*, at 115.

[122] *Ibid.*, at 115, *n*. 139.

[123] *Ibid.*, at 116.

[124] *Ibid.*, at 116, *n*. 140.

(v) Protected Transactions under the *Assignments and Preferences Act*

In preceding sections, discussion has focused on protected transactions under the *Fraudulent Conveyances Act*. As we have seen, however, section 4(1) of the *Assignments and Preferences Act* also deals with fraudulent conveyances. Under the latter Act, certain transactions cannot be successfully impeached, either because the requisite jurisdictional facts – arising by statute or under the case law – have not been proven, or because of the express exceptions to section 4(1) contained in section 5(1) of the Act.

a. Proof of Intent and Insolvency

(1) *Jurisdictional Facts under Section 4(1)*

It bears repeating that, in order to impeach a transaction under section 4(1), it must be shown not only that the debtor had a fraudulent intent, but also that the transaction was entered into by the debtor "when he is in insolvent circumstances or is unable to pay his debts in full, or knows that he is on the eve of insolvency".

(2) *The Knowledge or Intent of the Transferee*

It has been held that, in order to render a transaction void under the *Assignments and Preferences Act*, an impeaching creditor must show that the transferee had notice or knowledge of the debtor's fraudulent intent.[125] Whereas the matter of the transferee's "notice or knowledge" is made explicit in the *Fraudulent Conveyances Act*, a concurrent intent requirement is the result of a judicial gloss on the *Assignments and Preferences Act*. In *Johnson v. Hope*,[126] Maclennan J.A. attempted to explain the rationale as follows:[127]

> The statute, 13 Eliz. ch. 5, sec. 6, saves from its operation, [a] conveyance, &c., made upon good consideration, and *bona fide*, to persons not having at the time any *notice* or *knowledge* of the fraud or covin. It is remarkable that there is no similar general provision in our statute, R.S.O. ch. 124 [akin to the present *Assignments and Preferences Act*], saving transactions entered into without notice or knowledge of the intent or other circumstances which made them fraudulent. In one member alone, section 3(1) [now section 5(1)], the exception is extended to persons who are described as 'innocent purchasers or parties', which of course must mean persons without notice or knowledge.
>
> But then the word *bona fide* is used throughout, and it would seem to follow that the Legislature did not intend to involve persons having neither knowledge or notice, in the disabling and penal consequences of the acts

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[125] In some cases, reference has been made to notice or knowledge of the debtor's insolvency alone: see *Dana v. McLean* (1901), 2 O.L.R. 466 (App. Div.), at 470 and 471-72.

[126] *Johnson v. Hope* (1890), 17 O.A.R. 10. See *Ashley v. Brown*, *supra*, note 32, citing *Johnson v. Hope*.

[127] *Supra*, note 126, at 15-16 (emphasis in original).

> thereby forbidden. It would paralyse trade and mercantile business altogether, if transactions entered into in all honesty and good faith, and for valuable consideration, with persons apparently solvent and prosperous, were liable to be undone upon its being afterwards discovered and proved that such persons were at the time in embarrassed circumstances or unable to pay their debts in full. Such a construction of the Act would make it a trap and a snare instead of an enactment salutary and beneficial to the mercantile community. It has always been the policy of the law to protect, as far as possible, persons acting *bona fide*, and without notice of fraud or other wrong doing, and so I think a person who deals *bona fide* with an embarrassed debtor, and who at the time of the dealing has no knowledge or notice of his embarrassed condition, is safe from all the consequences enacted by the statute. It is hard to imagine how a transaction can be otherwise than *bona fide*, with reference to what is forbidden in this statute, if it has been entered into without knowledge or notice of the embarrassments of the debtor.
>
> I also think that as our statute is *in pari materia* with 13 Eliz. ch. 5, the 6th section of that Act may be held as applicable to the Ontario Act, so as to protect persons not affected with notice, and in that view the point may be regarded as decided by *Burns v. McKay*, 10 O.R. 167, (affirmed in this Court), and the cases there cited by the learned Chancellor.

However, some cases have refused to import concurrent intent into similar statutes.[128] In other cases, mere notice or knowledge of the debtor's fraudulent intent has not been sufficient to render a transaction invalid.[129] Quite clearly, then, the issue concerning the precise nature and scope of a transferee's involvement in the debtor's fraudulent scheme remains very much in doubt under the *Assignments and Preferences Act*.[130]

b. Transactions Protected under Section 5(1)

Notwithstanding that section 4(1) is expressly stated to be read "[s]ubject to section 5", only a portion of section 5 is applicable to fraudulent conveyances. The relevant portion is as follows:

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[128] See *Schwartz v. Winkler* (1901), 13 Man. R. 493 (K.B.); *Stephens v. McArthur* (1891), 19 S.C.R. 446, rev'g (1890), 6 Man. R. 496 (Q.B.); *Bank of Nova Scotia v. MacDonald* (1982), 41 C.B.R. (N.S.) 140 (N.B.S.C., T.D.); and *Federal Business Development Bank v. Van Klaveren*, *supra*, note 24. In the latter case, Barry J., by way of *obiter dictum*, adopted the principles enunciated by Dickson J. in *Hudson v. Benallack*, [1976] 2 S.C.R. 168, 21 C.B.R. (N.S.) 111 (subsequent references are to [1976] 2 S.C.R.), a preference case in bankruptcy. See *infra*, note 212 and supporting text, and *infra*, this ch., sec. 4(b)(ii)c.(1), concerning *Hudson*.

[129] See New Brunswick Report, *supra*, note 30, at 115, and discussion, *supra*, this ch., sec. 2(b)(iv)c.

[130] Moreover, the relationship between the transferee's intent and the proviso respecting the adequacy of consideration at the close of s. 5(1) of the *Assignments and Preferences Act*, *supra*, note 2, is equally ambiguous. See New Brunswick Report, *supra*, note 30, at 129-30:

> The effect of the proviso on the question of concurrent intent is uncertain. If the consideration is inadequate, it may be that only the intention of the debtor is relevant, the same as in the case where there is no consideration flowing to the debtor. On the other hand, if the concepts of concurrent intent and *bona fides* operate independently, inadequacy of consideration may not eliminate the requirement that the third party concur in the debtor's improper intent.

For a further discussion of this matter, see *ibid.*, at 130, *n*. 174.

> 5.-(1) Nothing in section 4 applies . . . to any *bona fide* sale . . . made in the ordinary course of trade or calling to an innocent purchaser . . . nor to any *bona fide* conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in consideration of a present actual *bona fide* payment in money, or by way of security for a present actual *bona fide* advance of money, or that is made in consideration of a present actual *bona fide* sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor.

Aside perhaps from some duplication,[131] the section 5(1) exceptions are relatively straightforward. Their reasonableness arises partly as a result of the operation of the proviso that "the money paid or the goods or other property sold or delivered [must] bear a fair and reasonable relative value to the consideration therefor". In effect, because of this proviso, the transactions to which section 5(1) make reference will not result in a lessening of the value of the debtor's assets available for his creditors. We shall now consider the nature and scope of the proviso.

(1) *"Good", "Valuable", and "Fair and Reasonable" Consideration*

In one critical respect, the task of the creditor who seeks to impeach a fraudulent conveyance is more difficult under the *Fraudulent Conveyances Act* than it is under section 4(1) of the *Assignments and Preferences Act*. In the former statute, there is no requirement concerning consideration other than that it be either "good" or "valuable" consideration; unless the consideration is grossly inadequate, the conveyance cannot be set aside on this basis alone. The latter statute differs sharply on this point. Section 5(1) extends protection to a *bona fide* transferee for value, but, as we have seen, contains a proviso that the consideration must be "fair and reasonable". The Nova Scotia case of *Leighton v. Muir*[132] illustrates the difference between the two provisions. In that case, an insolvent debtor conveyed property worth $8,500 to his sister, who agreed to assume the existing mortgage of $3,500. The Court held that the creditor could not succeed under 13 Eliz., c. 5, on the ground of inadequacy of consideration, but that he could succeed under *The Assignments and Preferences Act*[133] on precisely that ground, because of the express provision regarding adequacy of consideration. *Leighton v. Muir* suggests, then, that, under the Ontario *Assignments and Preferences Act*, inadequacy of consideration has the effect of relieving the creditor from proving concurrent intent on the part of the transferee.

(2) *Transactions to which the Proviso Makes Reference*

The New Brunswick Report stated that "[i]t is unclear whether the proviso in the provincial saving clause extends to all of the protected transactions or only to the category of transactions for a present consideration which immediately precedes it. Either interpretation is possible grammatically."[134] As a matter of logic, however, it is difficult to conceive of the proviso applying, for example, to an assignment for the general benefit of creditors, which is included in section 5(1). Therefore, if at least this occurrence is carved out of section 5(1) as an exception, then it is possible that other exceptions may have been intended. For example, it might be argued that the proviso does not apply to "any *bona fide* sale . . . made in the ordinary course of trade or calling to an innocent purchaser". If it does not apply, a merchant who knows he is on the eve of insolvency could not sell some goods at well below fair market value even for valid commercial reasons, such as an attempt to obtain needed capital in order to resurrect the business enterprise.[135]

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[131] For example, there may be some overlap between a "*bona fide* sale . . . made in the ordinary course of trade or calling" and a "*bona fide* conveyance . . . that is made in consideration of a present actual *bona fide* payment in money".

[132] *Supra*, note 84.

[133] R.S.N.S. 1954, c. 17.

(vi) Persons Having Standing to Impeach Fraudulent Conveyances

Whereas section 4(1) of the *Assignments and Preferences Act* provides that only transactions intended to defeat, hinder, delay, or prejudice a debtor's "creditors" are impeachable, section 2 of the *Fraudulent Conveyances Act* invalidates conveyances made with the intent to defeat, hinder, delay, or defraud "creditors or others". The effect of this distinction has been described succinctly in the New Brunswick Report as follows:[136]

> Since the English statute [13 Eliz., c. 5] refers to attempts to defeat 'creditors and others' it has been held that either a person who was a creditor at the time of the voidable transaction or a person who becomes a creditor subsequently may attack the transaction. Since the provincial legislation refers to

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[134] New Brunswick Report, *supra*, note 30, at 128-29.

[135] Other Canadian jurisdictions offer alternative ways of structuring the provision akin to s. 5(1). In some cases, the manner in which the provision is drafted may make its interpretation somewhat easier. For example, the relevant provision in the Manitoba *Assignments Act*, R.S.M. 1970, c. A150, reads:

> 44. Nothing in sections 38 to 43 applies
>
> . . . .
>
> (*b*) to
>
> (i) a bona fide sale or payment made in the ordinary course of trade or calling to an innocent purchaser or party; or
>
> (ii) a payment of money to a creditor; or
>
> (iii) a bona fide conveyance, assignment, transfer, or delivery over of goods, securities, or property of any kind, as above mentioned, that is made in consideration of a present actual bona fide payment in money, or by way of security for a present actual bona fide advance of money, or that is made in consideration of a present actual bona fide sale or delivery of goods or other property;
>
> if the money paid, or the goods or other property sold or delivered, bear a fair and reasonable relative value to the consideration therefor.

See, also, *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18, s. 6.

[136] New Brunswick Report, *supra*, note 30, at 140-41.

attempts to defeat 'creditors', only a person who is a creditor at the time of the voidable transaction may attack the transaction.

a. Standing under the Fraudulent Conveyances Act

(1) *Existing Judgment Creditors*

Quite clearly, creditors who have judgment at the time of the conveyance may seek to impeach an allegedly fraudulent transaction. A writ of execution is not essential for this purpose.[137]

(2) *Non-Judgment Creditors*

It would seem to be reasonably well established that a non-judgment creditor or claimant can attack a conveyance under the *Fraudulent Conveyances Act* without first obtaining judgment.[138] However, it has been said that, "[t]hough it is unnecessary for a plaintiff in an action to set aside a conveyance as a fraud on creditors to prove that he has reduced his claim to judgment, he must nevertheless prove that he has in fact a valid claim against the transferor and it will not be assumed that he has such a claim merely because he has asserted it by bringing another action which is still pending".[139]

Where a conveyance is effected with a clear view to defeating persons with claims that ultimately may be reduced to judgment, courts usually have exhibited no hesitation in allowing the claimants to impeach the conveyance. Generally speaking, this attitude prevails whether or not the plaintiff's claim is liquidated.[140] In *Kapicki v. Andriuk*,[141] the plaintiffs had commenced an action for damages caused to their lands by flooding resulting from the construction of a dam by the defendants. In *Murdoch v. Murdoch*,[142] a wife filed a counter-petition for divorce and maintenance.[143] In *Rider v. Kidder*,[144] a husband had covenanted to pay his wife a sum of money should she survive him. In these and other similar cases, the claimants were held to have standing under applicable fraudulent conveyances legislation.

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[137] See *Brown v. Weil* (1927), 61 O.L.R. 55, at 59, [1927] 4 D.L.R. 218, at 220 (App. Div.); *Shephard v. Shephard* (1925), 56 O.L.R. 555 (App. Div.); and *Longeway v. Mitchell* (1870), 17 Gr. 190.

[138] See New Brunswick Report, *supra*, note 30, at 145 and 146; *Hopkinson v. Westerman* (1919), 45 O.L.R. 208, 48 D.L.R. 597 (S.C., App. Div.); *Ferguson v. Lastewka*, *supra*, note 45; and *May on Fraudulent and Voluntary Conveyances* (3d ed., 1908), at 102.

[139] *Owen Sound General and Marine Hospital v. Mann*, *supra*, note 48, *per* Anger J., citing *Bell v. Williamson*, [1945] O.R. 844, [1946] 1 D.L.R. 372 (C.A.). *Halsbury's Laws of England* (4th ed., 1977), Vol. 18, at 177, *n*. 3, reads, in part: ". . . it is difficult to see how the present statutory provision [*Law of Property Act 1925*, s. 172] . . . can be operated in favour of a person who does not have a quantifiable monetary claim of some kind at the time proceedings are commenced under that provision". Section 172(1) refers broadly to conveyances voidable at the instance of "any person thereby prejudiced".

[140] Although, in a minority of cases, courts have held that persons with unliquidated claims are not "creditors" under the *Fraudulent Conveyances Act*, and that, while within the strict wording of the statute, they can bring their action only upon recovering judgment. See *Cameron v. Cusack*, *supra*, note 101, at 493; *Bank of Montreal v. Crowell*, *supra*, note 24, at 304; New Brunswick Report, *supra*, note 30, at 144-45, citing *Ashley v. Brown*, *supra*, note 32; *Gurofski v. Harris* (1896), 27 O.R. 201 (H.C.J.), aff'd (1896), 23 O.A.R. 717 (subsequent reference is to 27 O.R.); and *Faulhaber v. Ulseth* (1976), 66 D.L.R. (3d) 488, at 499, [1976] 4 W.W.R. 48, at 54 (Alta. S.C., T.D.).

[141] *Supra*, note 45.

A somewhat vexing question has arisen concerning entitlement to sue where the claim against the debtor is remote or very highly speculative. In *Ferguson v. Lastewka*,[145] while, at the time of the impeached conveyance, no damage action had yet been commenced in respect of an accident involving the debtor and the plaintiff, the debtor had been convicted of an offence in connection with the accident and was already in custody immediately prior to the date of the conveyance. The trial judge was of the view that, since the accident victim had a cause of action against the debtor and was "likely" to sue, he could attack the transaction.

In many of the cases, there is no explicit consideration of the relationship between the debtor's intent and the likelihood of the claim being pressed to a successful conclusion, although the relationship is very close indeed. Where the claim is so remote or frivolous or highly speculative that it has been virtually forgotten or reasonably ignored by the debtor, it has often been inferred that he had no fraudulent intent. In *Gurofski v. Harris*,[146] for example, MacMahon J. noted that the action for slander brought by the plaintiff "was apparently regarded as so frivolous and of such little moment that settlement even on those terms [$25] was declined".[147]

However, in *In re Ridler, Ridler v. Ridler*,[148] a case involving a guarantee given by the debtor, Cotton L.J., appearing to take a somewhat more "objective" view of what is required of a debtor, stated as follows:

> Then as to the point that the settlor was not indebted, but only subject to a liability which might never become a debt. A man is not at liberty to take a sanguine view, but is bound to act upon a reasonable view of what is likely to happen. In the circumstances of this case, *any reasonable man* must have looked upon this guarantee as one which would probably be enforced, and the settlement must be taken as made with intent to delay or hinder creditors.

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[142] (1976), 1 Alta. L.R. (2d) 135, [1977] 1 W.W.R. 16 (S.C., T.D.).

[143] See, also, *MacDonald v. MacDonald*, [1957] O.W.N. 419, 10 D.L.R. (2d) 309 (H.C.J.), where it was held that a divorced wife holding a judgment for maintenance may impeach her ex-husband's fraudulent conveyance, notwithstanding that no money was owing at the time of the conveyance. The ex-wife was held to be one of the "others" contemplated by the Act. See New Brunswick Report, *supra*, note 30, at 145, *n*. 211.

[144] (1805), 10 Ves. 360, 32 E.R. 884 (Ch.).

[145] *Supra*, note 45.

[146] *Supra*, note 140.

[147] *Ibid.*, at 207. In *Cameron v. Cusack*, *supra*, note 101, at 491, reference was made by Hagarty C.J.O. to the situation where the debtor "is threatened with an action for some tort, the result of which is wholly speculative, both as to its success or defeat, or in the possible amount of damages".

[148] *Supra*, note 34, at 82 (emphasis added).

Lord Selborne L.C. rejected the view that the assets of the person primarily liable should be taken into account by the Court in assessing the likelihood that the debtor would be called upon under his guarantee; rather, the Court must proceed on the assumption that the principal debtor is unable to pay. He then went on to say, "I do not say that there might not be a state of things in which the liability of the guarantor might be so remote that it need not be regarded".[149]

(3) *Secured Creditors*

A secured creditor is not entitled to impeach a transaction under the *Fraudulent Conveyances Act*,[150] unless the property secured is not sufficient to satisfy the debt owing to him, in which case the secured creditor will be a "creditor" under the Act to the extent of the deficiency.[151] A fully secured creditor does not look to the general assets of the debtor in order to satisfy his debt. The burden of proving the existence of a deficiency rests on the secured party;[152] in the absence of evidence to the contrary, it has been presumed that the security is sufficient.[153]

It is clear that the operative date at which to assess the status of the security is the date of the conveyance.[154] If, however, a deficiency arises subsequent to the conveyance, the secured creditor is in the position of a subsequent creditor,[155] a matter to be considered below. In *Crombie v. Young*,[156] a solvent debtor made a voluntary settlement subsequent to a mortgage. The mortgagee was satisfied that the value of the mortgaged property was considerably in excess of the loan. However, at the date the mortgage matured, the real estate market had fallen to the extent that the secured creditor no longer was fully secured. The mortgagee sought to impeach the transaction. The settlement was upheld, and MacMahon J. stated as follows:[157]

> If at the time a mortgage is given, payable, say in five years, the mortgaged property is regarded by both the mortgagor and mortgagee as ample security for the mortgage debt, then if the mortgagor cannot make a voluntary settlement (although otherwise financially in a position so to do), because he may possibly become a debtor to the mortgagee by reason of the depreciation of the mortgaged property, just before the expiration of the five years, the argument must hold good as to a mortgage having ten years to run, and a like result happening.

It should be noted that, as a matter of causation alone, the effect of the settlement was to prejudice the secured creditor: if the settlement had not been made, the secured creditor could have had access to the property in question. It is, of course, not uncommon to encounter cases in which, through unforeseen circumstances, a debtor ultimately is rendered insolvent by means of a transaction made without fraudulent intent and when the debtor was solvent.[158] However, the precise nexus between the conveyance and its effect on a person who is not a creditor at the date of the conveyance is often difficult to discern.

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[149] *Ibid.*, at 80.

[150] See *Arnold v. Fleming*, [1923] 1 D.L.R. 1026, [1923] 1 W.W.R. 706 (Alta. S.C., T.D.), and *McLean v. Ratekin*, *supra*, note 40.

[151] See *Sun Life Assurance Co. of Canada v. Elliott*, *supra*, note 57.

[152] See *Re Skinner* (1960), 27 D.L.R. (2d) 74 (B.C.S.C.).

[153] See *Anderson v. Serge* (1924), 18 Sask. L.R. 255, [1924] 2 D.L.R. 1018 (C.A.).

[154] See *Crombie v. Young* (1894), 26 O.R. 194 (C.P. Div.), at 200 and 202.

[155] See *Gauthier v. Woollatt*, *supra*, note 97.

[156] *Supra*, note 154.

[157] *Ibid.*, at 207.

Before leaving our discussion of secured creditors, it should be pointed out that nothing prevents a secured party from suing on the debtor's convenant to pay and, upon recovering judgment, becoming a creditor within the meaning of both provincial statutes.[159] However, as stated, it would appear that, if the deficiency arose subsequent to the impugned transaction, the creditor would be a subsequent creditor. As such, he would be under some disabilities, discussed below, not suffered by judgment creditors who existed at the date of the transaction.

(4) *Subsequent Creditors*

Another class of persons likely precluded from bringing an action under the *Assignments and Preferences Act*, but having standing to sue under the *Fraudulent Conveyances Act*, is that of subsequent creditors, that is, persons who become creditors subsequent to the transaction sought to be impeached.

However, even under the *Fraudulent Conveyances Act*, a distinction has arisen between existing and subsequent creditors with respect to their entitlement to bring an action. The rationale for such a distinction has been stated as follows:[160]

> The ease of proving fraud, an issue in every fraudulent conveyance case, has brought about a difference in the rights of the two principal types of claimants. It is easy to see why this is true. The task of showing the effect of a debtor's diminution of his present estate upon his ability to meet existing obligations is relatively simple. But once the transaction is completed, it is much more difficult to connect it with some future liability. If the subsequent debt arose a great length of time afterward, the connection is especially difficult to show. Something must be found which justifies the statement that the debtor intended to injure the future creditor.

The decision in *Gauthier v. Woollatt*[161] fairly sums up the general rule. In that case, Roach J. held that a subsequent creditor may successfully impeach a fraudulent conveyance under the *Fraudulent Conveyances Act* in two circumstances: (1) if, at the institution of the action, there still remains unpaid a creditor whose claim existed at the date of the conveyance,[162] at least where the existing creditor himself would have been entitled to impeach the conveyance;[163] or (2) if the debtor's purpose was to put his assets beyond the uncertainties of business – that is, if his motive was to defraud subsequent creditors generally.[164]

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[158] See *Elgin Loan and Savings Co. v. Orchard*, *supra*, note 62, and *McGuire v. The Ottawa Wine Vaults Co.*, *supra*, note 38. See, also, *Fleming v. Edwards*, *supra*, note 86.

[159] See *Parr v. Montgomery* (1880), 27 Gr. 521.

[160] Walden, "Creditors' Rights: Conveyances in Fraud of Subsequent Creditors" (1952), 40 Ky. L. J. 433, at 437.

[161] *Supra*, note 97.

The latter situation would cover cases like *The Ottawa Wine Vaults Co. v. McGuire*,[165] where the debtor, engaged in a hazardous business and knowing that he would become indebted, attempted to remove his assets from the reach of future creditors. Many of the cases have focused on the debtor's "hazardous" or "speculative" enterprise as evidencing knowledge that considerable debts probably would be incurred.[166] On the other hand, there are many other cases that make it clear that the debtor need not have entered into a hazardous undertaking in order for subsequent creditors to invoke the statute. This broader rule has been stated in *Newlands Sawmills Co. v. Bateman*[167] by Martin J.A., who, after discussing the decision of Sir R. Malins V.C. in *Mackay v. Douglas*,[168] stated:[169]

> It thus becomes apparent that the principle is based upon the contemplated entry into a trading or other venture which 'might' lead to indebtedness merely, *and it is not necessary that the business should be of a hazardous nature*, and the use of that expression in the headnote [to *Mackay v. Douglas*] in the Law Reports, and the consequent restriction of the principle to the special class of hazardous undertakings is not justified by anything in the judgment when it is closely examined, though it is true that the firm in which Douglas became a partner had been to his knowledge, and continued to be engaged in speculations in jute which made the business of a 'rather reckless nature' as the Vice Chancellor said L.R. 14 Eq. at p. 120 nevertheless, the result would have been the same upon the 'broad ground' clearly laid down if insolvency had resulted as one of the ordinary risks of the partnership's business operations, quite apart from the jute speculations. The headnotes in the other three reports property [*sic*: properly] omit this restriction and simply state the principle upon the *broad ground of a voluntary settlement executed on the eve*

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[162] See *Bludoff v. Osaschoff*, *supra*, note 56; *Collard v. Bennett* (1881), 28 Gr. 556, at 559; *Cromwell v. Comeau*, *supra*, note 83, at 684 and 685; *Masuret v. Mitchell* (1879), 26 Gr. 435, at 441, *per* Spragge C., at 442, *per* Blake V.C., and at 443, *per* Proudfoot V.C.; *McGuire v. The Ottawa Wine Vaults Co.*, *supra*, note 38; *Ewachowski v. Marchischuk*, [1917] 3 W.W.R. 747 (Man. K.B.); and *Buckland v. Rose*, *supra*, note 57.

See, also, Note, "Conveyances in Fraud of Subsequent Creditors" (1924), 37 Harv. L. Rev. 489, at 490, and C.H.F., "Fraudulent Conveyances – Right of Subsequent Creditor to Set Aside Voluntary Conveyance" (1928), 22 Ill. L. Rev. 673.

[163] In *Dancey v. Brown* (1914), 19 D.L.R. 862, at 865, 31 O.L.R. 152, at 155-56 (App. Div.), Mulock C.J. Ex. stated that, "if such prior creditors are not entitled to impeach the conveyances, neither is the plaintiff, who is a subsequent creditor, for his equity is no higher than that of the prior creditors".

[164] See *Ewachowski v. Marchischuk*, *supra*, note 162, and *Collard v. Bennett*, *supra*, note 162.

[165] *Supra*, note 57.

[166] See *Crombie v. Young*, *supra*, note 154, at 203.

[167] *Newlands Sawmills Co. v. Bateman* (1922), 70 D.L.R. 165, [1922] 3 W.W.R. 649 (B.C.C.A.) (subsequent reference is to 70 D.L.R.).

[168] *Supra*, note 57.

[169] *Supra*, note 167, at 171 (emphasis added).

> *of going into trade*. It is desirable to notice this error because the Law Report's headnote was adopted by Garrow, J.A., in the Court of Appeal for Ontario in *McGuire's* case, 8 D.L.R. at pp. 230-231, 27 O.L.R. at p. 322 without reference to the other reports which are of equal authority; . . .

While the above observations are likely *obiter*, since the Court held that the business was in fact "hazardous", they do reflect a less restrictive rule that seems both more logical and consistent with the present fundamental requirement under the *Fraudulent Conveyances Act* to prove the fraudulent intent of the debtor. A debtor may well have such an intent notwithstanding his entry into a business enterprise that cannot be characterized as "hazardous".[170] In fact, it has been held that a conveyance made for the purpose of evading future creditors in general[171] or a specific future creditor[172] is fraudulent and void, whether the debtor is indebted at the time or not.[173]

Earlier, it was stated that the decision in *Gauthier v. Woollatt*[174] specified two circumstances in which a subsequent creditor could impeach a fraudulent conveyance. However, reference also should be made to a third situation described, and apparently dismissed, by Roach J. in the above case. Roach J. stated:[175]

> May on Fraudulent and Voluntary Conveyances, 3rd ed., p. 43, speaks of a third class as follows: 'If the conveyance has been made with the actual intention of delaying, hindering or defrauding the grantor's existing creditors and although subsequent creditors do not appear to have been in his contemplation at the time it seems that the conveyance will be void as against subsequent creditors who are delayed, hindered or defrauded as a necessary result of the conveyance *even though, in the meantime, the claims of existing creditors have been satisfied*.'

In discussing the debtor's "purging" of his fraudulent intent by the payment of existing creditors, as well as the difficulty encountered where subsequent creditors are involved, Roach J. said:[176]

> In the absence of decided authority to the contrary, it would seem to me that a settlor who, in embarrassed financial circumstances, makes a settlement

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[170] Unless, perhaps in order to fit within the rigid formula, "hazardous" is used so loosely as to connote any business likely to promote reasonably heavy liabilities. In *Jeffrey v. Aagaard*, *supra*, note 56, at 1206, Dennistoun J.A. stated that the "restaurant business is a hazardous business inasmuch as it depends very largely upon the character of the management".

[171] See *Stileman v. Ashdown* (1742), 2 Atk. 477, at 481, 26 E.R. 688, at 690, aff'd (1743), 2 Atk. 608, 26 E.R. 763 (Ch.); *Arnold v. Fleming*, *supra*, note 150; *Newlands Sawmills Co. v. Bateman*, *supra*, note 167; *Crombie v. Young*, *supra*, note 154; *Collard v. Bennett*, *supra*, note 162, at 559; and *Campbell v. Chapman* (1879), 26 Gr. 240, at 242-43.

[172] See *Bludoff v. Osaschoff*, *supra*, note 56, and *Ewachowski v. Marchischuk*, *supra*, note 162.

[173] See *Buckland v. Rose*, *supra*, note 57.

[174] *Supra*, note 97.

[175] *Ibid.*, at 280 (emphasis added).

[176] *Ibid.*, at 282.

admittedly for the purpose of protecting the property thereby settled against the claims of existing creditors, purges his fraud by paying those creditors, provided, of course, that, in paying them, he does not substitute new creditors for the old ones.[177] Even though his earlier generosity had been at the expense of his justice toward his creditors, having paid those creditors and thereby discharged his legal and moral obligation to them and having none others in contemplation, is the conveyance to be forever regarded as contaminated? In my opinion this is not so. By a turn in the wheel of fortune the settlor, instead of wincing under the pinch of financial distress, may become fabulously wealthy. He still desires that the beneficiary of his earlier generosity should enjoy the gift. If it is tainted what could or should the settlor do to purify it? Is he to cause it to be reconveyed to himself and then, simply because he is now in a position to make the gift without any suggestion of fraudulent intent being imputed to him, make a new conveyance thereof to the beneficiary? These would be idle motions and, because they are lacking, is the gift in the hands of the beneficiary to be subject to attack by a subsequent creditor in the event that evil days again overtake the settlor? I do not think that was the purpose or intent of the statute.

b. Standing under the Assignments and Preferences Act

In the preceding section, we discussed the entitlement of "creditors and others" to sue under the *Fraudulent Conveyances Act*. In this section, reference will be made to the standing of "creditors" to impeach a fraudulent conveyance under section 4(1) of the *Assignments and Preferences Act*. Under the latter statute, persons with unliquidated claims do not become "creditors" until their claims are reduced to judgment.[178] Moreover, it has been stated time and again that only creditors existing at the time of the impeached conveyance can avoid it – an orthodox view represented, for example, by *Ashley v. Brown*.[179] However, the New Brunswick Report was not entirely happy with this view. It stated:[180]

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[177] Concerning the substitution of new creditors for old ones, see New Brunswick Report, *supra*, note 30, at 146: "There may indeed be a general rule that a creditor whose claim really amounts to a substitution of one creditor for another by the debtor can attack a transaction as if he were in the position of the original creditor for which he has been substituted." After citing *Gauthier v. Woollatt*, *supra*, note 97, in support of this proposition, the Report continued (at 146, *n*. 214): "Since this rule is stated only in dicta, it is not certain whether it extends only to cases in which the new creditor would by law be subrogated to the rights of the former creditor, as in the case of the guarantor, or whether it might extend generally to cases in which the debtor pays off former creditors with the proceeds of credit obtained from new creditors." If, however, a subsequent creditor is entitled to impugn a transaction where the debtor intends to defeat him by means of the transaction, then the subsequent creditor would be protected.

[178] See *Ashley v. Brown*, *supra*, note 32. See, also, *Gurofski v. Harris*, *supra*, note 140. It should be noted that, while these cases dealt with the meaning of "creditors" under s. 4(2), the preference portion of the *Assignments and Preferences Act*, the relevant statutory language is identical to that in s. 4(1). See, *Perkins Electric Co. v. Orpen* (1921), 21 O.W.N. 135 (App. Div.), aff'd (1922), 70 D.L.R. 397 (S.C.C.). See, also, by way of analogy, *Faulhaber v. Ulseth*, *supra*, note 140, where the Court considered, *inter alia*, r. 383 of the Alberta Supreme Court Rules, Alta. Reg. 390/68, which dealt with conveyances to defraud "creditors or a creditor". Steer J. affirmed the interpretation of the term "creditor" to exclude persons suing for a tort.

[179] *Supra*, note 32. See, also, *Gurofski v. Harris*, *supra*, note 140. However, in *Gurofski v. Harris*, Boyd C. stated (*supra*, note 140, at 205) that, "as a subsequent creditor by judgment, the plaintiff cannot attack a prior deed for adequate value where no debts still unpaid were existing at the time of the execution of the deed, for it is not shewn that the transaction was colourable or entered into with a view to incur future obliga-

> *Ashley v. Brown* . . . if followed strictly, would indicate that a subsequent creditor can never attack a transaction under the provincial legislation, even if it is devised as a scheme for the specific purpose of defeating his claim. Such a holding may not have been necessary to decide the case.

(vii) The Status of Transferees

a. Tracing the Property and Proceeds

We have noted already that, notwithstanding the use of the term "void" in the two provincial statutes under discussion, a transaction that contravenes either statute is voidable only. If, before the transaction is avoided, the original transferee conveys the property to a *bona fide* purchaser for value without notice of the original fraud, the second conveyance is valid.[181] However, where the second transferee is not a *bona fide* purchaser for value and without notice, the property can be recovered.[182]

With respect to the tracing of proceeds of a sale by the original transferee to a subsequent transferee, older Ontario cases refused to grant impeaching creditors the right to follow the proceeds.[183] However, these cases were overruled by *Westinghouse Canada Ltd. v. Buchar*.[184] In that case, the Court was asked to consider the application to a *Fraudulent Conveyances Act* proceeding of section 12 of the *Assignments and Preferences Act* – the provision, unique to the latter statute, that permits the tracing of proceeds into the hands of an original transferee.[185] In *Westinghouse Can-*

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tions . . .". Notwithstanding that the case dealt with a preference, the precise application of this statement is somewhat intriguing in light of the orthodox learning, described above, concerning the meaning of "creditors" under the *Assignments and Preferences Act*. It also should be noted that Boyd C.'s formulation of the rule in the second sentence corresponds exactly to the general rule regarding subsequent creditors seeking to invoke 13 Eliz., c. 5, or the *Fraudulent Conveyances Act*.

[180] New Brunswick Report, *supra*, note 30, at 142, *n*. 206.

[181] See *Marshall-Wells Alberta Co. Ltd. v. Sauve* (1958), 25 W.W.R. 610 (B.C.S.C.), citing *Morewood v. S. Yorkshire Ry. and River Dun Co.* (1858), 3 H.& N. 798, 28 L.J. Ex. 114, 157 E.R. 690 (Ex.). See, also, *Cameron v. Moseley* (1923), 56 N.S.R. 300, [1923] 3 D.L.R. 267 (S.C.); *Tennant & Company v. Gallow* (1894), 25 O.R. 56 (H.C.J.), at 59; and *Totten v. Douglas* (1871), 18 Gr. 341.

[182] *Buchanan v. Dinsley* (1865), 11 Gr. 132. It should be noted that the New Brunswick Report has commented that s. 6 of 13 Eliz., c. 5, akin to ss. 3 and 4 of our *Fraudulent Conveyances Act*, was intended to protect a subsequent, and not an original, transferee: see *supra*, note 30, at 115, *n*. 139. The cases, however, support the proposition that the saving clause refers to the transaction between the debtor and the original transferee: see Dunlop, *supra*, note 39, at 525, *n*. 15. This interpretation seems consistent with the construction of the *Fraudulent Conveyances Act*: s. 2 renders certain conveyances between a debtor and his transferee invalid and ss. 3 and 4 operate as saving provisions.

[183] See *Gray v. Quinn*, *supra*, note 26. See, also, *Stuart v. Tremain* (1882), 3 O.R. 190 (Ch. Div.), and *Robertson v. Holland* (1888), 16 O.R. 532 (C.P. Div.).

[184] *Supra*, note 26. This case followed the Manitoba case of *John Deere Ltd. v. Paddock*, [1973] 2 W.W.R. 116 (Man. C.A.). It has been held in Nova Scotia that the impeaching creditors can follow the proceeds into the hands of the original transferee: see *Cameron v. Moseley*, *supra*, note 181.

[185] Section 12 is reproduced *supra*, at 128-29.

ada Ltd. v. Buchar, the argument was successfully made that the operation of section 12 should not be read restrictively but should extend to cover transactions made "invalid against creditors" by the *Fraudulent Conveyances Act*. Lacourcière J.A. stated that "the plain intention of the statutes, to be read together, is to constitute the fraudulent transferee a trustee of the proceeds replacing the lands, for the benefit of the defrauded creditors".[186]

It should be noted that the New Brunswick Report referred to authority for the proposition that, if the proceeds are commingled with or exchanged for other property so that they cannot be distinguished, they cannot be traced.[187] The applicability of the decisions cited in the New Brunswick Report is, however, uncertain in light of section 12 of the Ontario *Assignments and Preferences Act*. It would seem that section 12 is wide enough to cover all situations, regardless of whether the proceeds are readily distinguishable. Section 12(1) provides that "the money or other proceeds may be seized or recovered in an action". Section 12(2) provides for the seizure of "proceeds [that] are of such a character as to be seizable under execution". Section 12(3) provides for the recovery of proceeds "whether the proceeds are or are not of such a character as to be seizable under execution". Given these three subsections, it is certainly arguable that the proceeds need not be kept distinguishable from the transferee's other property in order to be followed by impeaching creditors. Unfortunately, the issue has not been resolved, although cases determined under 13 Eliz., c. 5, which contains no provision akin to section 12, are clearly suspect.

Finally, the New Brunswick Report also cited cases that have held that, where proceeds arise in a manner other than through a sale or other similar disposition of the property, such proceeds cannot be followed.[188] In *Bellhouse v. Wong*,[189] the debtor sold property to a transferee, who then placed on the property a policy of fire insurance. Thereafter, a creditor successfully impeached the conveyance, but the goods had been destroyed and the transferee had collected insurance proceeds. The Court held that the insurance proceeds could not be seized by the creditor. The transferee had no duty to insure on behalf of the creditor, who was a stranger at the time the insurance was effected. However, the Court did suggest that "the matter might be doubtful" where insurance was taken out subsequent to the judgment voiding the conveyance, since the creditor would have an interest in the insured property. A rationale for this treatment of insurance proceeds was given in *Canadian Credit Men's Trust Association Ltd. v.*

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[186] *Westinghouse Canada Ltd. v. Buchar*, *supra*, note 26, at 141.

[187] New Brunswick Report, *supra*, note 30, at 137. In *J.R. Watkins Medical Co. v. Gray*, [1920] 2 W.W.R. 588 (Alta. S.C., T.D.), the debtor transferred personal property to his wife who, in the course of the business, sold the property and used the proceeds to purchase further inventory. The Court held that the property then in the possession of the wife was not a substitution for the original property and was not earmarked in such a way as to be held in trust for the creditors. It was impossible to say which part of the present stock-in-trade was a direct result of the original sale.

[188] New Brunswick Report, *supra*, note 30, at 137.

[189] *Bellhouse v. Wong* (1941), 56 B.C.R. 455, [1941] 4 D.L.R. 56, [1941] 3 W.W.R. 503 (C.A.).

Chow Lun,[190] by Walsh J.:[191]

> This is not a case of following the proceeds of the sale of an article which was made the subject of a fraudulent transfer into the hands of the transferee. If it was, the legal position would be vastly different. The fund which it is sought to attach was created, not by a sale or other disposition of the car, but by its destruction, and it arose out of a contract of indemnity between the transferee and the insurance company. She had an insurable interest in the car which she was entitled to protect against loss by fire, as she did. I do not think that her husband's creditors are entitled to the benefit of this contract simply because the subject-matter of it was transferred to her in fraud of them. I have no quarrel with the authorities cited to me by Mr. Gow as to the exigibility of money payable under a fire-insurance policy but they do not touch the point as they all deal with insurance effected by the debtor himself and not by his transferee. His argument that Mrs. Chow was a trustee of this car for her husband and so his creditors are entitled to follow this insurance money into her hands cannot be given effect to. She was not a trustee of it at all. She was as between him and her the absolute owner of it. The judgment of the Court of Appeal in *Rayner v. Preston* (1881) 18 Ch. D. 1, 50 L.J. Ch. 472, 44 L.T. 787, for a reference to which I am indebted to my brother Ford, bears out, I think, the view which I have expressed as to Mrs. Chow's right to this money because it comes to her under her contract of indemnity with the insurance company. The only object in bringing this action was to secure this insurance money for the car had been destroyed before it was commenced and a mere declaration as to the fraudulent character of the bill of sale to her would avail the plaintiff nothing.

Yet, notwithstanding the arguments marshalled in the above two cases, and leaving aside the payment of insurance premiums by the transferee, at the end of the day the transferee had acquired proceeds that could not have been kept if the property had been "sold or disposed of, realized or collected", as provided in section 12(1) of the *Assignments and Preferences Act*.

b. Compensation for Transferees

It is clear that, following the impeachment of a conveyance, the transferee will not be automatically compensated for the consideration he has given up. After noting "this somewhat harsh result", the New Brunswick Report stated:[192]

> Probably it is this consequence which makes courts reluctant to set aside conveyances under the proviso to section 3(1) of the provincial legislation on the grounds that the consideration is inadequate. . . .
>
> It may be that a third party who gave valuable consideration could take an action for money had and received to get back the consideration that he

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[190] *Canadian Credit Men's Trust Association Ltd. v. Chow Lun*, [1931] 1 D.L.R. 1000, [1931] 1 W.W.R. 211 (Alta. S.C.) (subsequent reference is to [1931] 1 W.W.R.).

[191] *Ibid.*, at 211-12. (The quotation is not fully reproduced in [1931] 1 D.L.R.).

[192] New Brunswick Report, *supra*, note 30, at 138, *n*. 196. The Report noted (*ibid.*) that "[t]he preferred creditor does not face this problem because the original debt would not be affected by the illegality of the preference".

gave. The problem is whether the courts would grant him a remedy in view of the illegality[193] of the transaction.

3. FRAUDULENT OR UNJUST PREFERENCES

(a) THE COMMON LAW POSITION

It has been observed that, in the absence of legislation respecting fraudulent preferences – that is, transfers of property to a creditor in fraud of other creditors – preferences *per se* are not invalid.[194] The rationale for a *laissez-faire* approach to priorities given to some creditors – for example, by means of preferences – has been expressed as follows:[195]

> The elimination of priorities in this context is not as simple a matter as may initially appear. Direct payment made by a debtor to a creditor is the normal, and by far the most frequent, method through which the claims of creditors are satisfied. It would be undesirable to place restrictions on direct payment when it occurs as a matter of normal business practice. Legislative interference in the direct payment process might be justified, however, when the circumstances of the debtor are such that administrative involvement in his affairs is required in order to ensure that all creditors are treated fairly.

(b) PREFERENCES UNDER THE *FRAUDULENT CONVEYANCES ACT*

Notwithstanding the broad language of 13 Eliz., c. 5, and the *Fraudulent Conveyances Act*, the orthodox learning is that these Acts have "no regard whatever to the question of preference or priority among creditors";[196] a preference simply "is not avoided"[197] by these statutes. Neither statute is intended "to provide equal distribution of the estates of debtors among their creditors . . .".[198]

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[193] *Quaere* the characterization of the transaction as "illegal". Not all void or voidable contracts are illegal, and the right to recover money paid may vary, depending on the type of transaction.

[194] See *Ex parte Griffith* (1883), 23 Ch. D. 69; *Johnson v. Hope*, *supra*, note 126, at 14; and *Toronto-Dominion Bank v. Michael*, *supra*, note 86.

[195] Law Reform Commission of British Columbia, *The Enforcement of Judgment Debts: The Creditors' Relief Act* (Working Paper No. 21, n.d.) (hereinafter referred to as "B.C. Working Paper"), at 52. The B.C. Working Paper dealt with fraudulent preferences in the context of a consideration of payments made by debtors to creditors that are not caught by the British Columbia creditors' relief legislation.

[196] *Ferguson v. Lastewka*, *supra*, note 45, at 583. (The above quotation does not appear in [1946] O.W.N. 685.)

[197] *Ashley v. Brown*, *supra*, note 32, at 503. See, also, *Mulcahy v. Archibald*, *supra*, note 79, and *Hopkinson v. Westerman*, *supra*, note 138.

[198] *Cameron v. Cusack*, *supra*, note 101, at 494, quoting Fry J. in *In re Johnson, Golden v. Gillam*, *supra*, note 103, at 392. See, also, *Gurofski v. Harris*, *supra*, note 140, at 205. This view should be contrasted with the view often given of the *Assignments and Preferences Act*. In *River Stave Co. v. Sill* (1886), 12 O.R. 557 (Q.B.), at 567, Armour J. stated:

> The object and intention of the Legislature in passing the Act 48 Vic. ch.26(O.) [see *supra*, note 20] was to compel, so far as it had the power, all persons in insolvent circumstances or unable to pay their debts in full, or knowing themselves to be on the eve of insolvency, to treat all their creditors alike by making such a disposition of their assets as would pay all their creditors their just debts ratably and proportionably, and without preference or priority.

(c) THE LEGISLATIVE FRAMEWORK

Specific fraudulent preference legislation exists in all provinces except Newfoundland.[199] In Ontario, fraudulent preferences are dealt with in the *Assignments and Preferences Act*. The relevant sections provide as follows:

> 4.-(2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his debts in full, or knowing himself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over his other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.
>
> (3) Subject to section 5, if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, it shall, in and with respect to any action or proceeding that, within sixty days thereafter, is brought, had or taken to impeach or set aside such transaction, be presumed *prima facie* to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure.
>
> . . . .
>
> (5) The word 'creditor' in the fifth line of subsection (2) [and] in the second line of subsection (3) . . . includes any surety and the endorser of any promissory note or bill of exchange who would upon payment by him of the debt, promissory note or bill of exchange, in respect of which such suretyship was entered into or such endorsement was given, become a creditor of the person giving the preference within the meaning of those subsections.
>
> 5.-(1) Nothing in section 4 applies . . . to any *bona fide* . . . payment made in the ordinary course of trade or calling to an innocent . . . person, nor to any payment of money to a creditor, nor to any *bona fide* conveyance, assignment, transfer or delivery over of any goods or property of any kind . . . by way of security for a present actual *bona fide* advance of money, or that is made in consideration of a present actual *bona fide* . . . delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor.
>
> (2) In the case of a valid sale of goods or other property and payment or transfer of the consideration or part thereof by the purchaser to a creditor of the vendor under circumstances that would render void such a payment or transfer by the debtor personally and directly, the payment or transfer, even though valid as respects the purchaser, is void as respects the creditor to whom it is made.
>
> . . . .
>
> (4) Where a payment has been made that is void under this Act and any valuable security was given up in consideration of the payment, the creditor is entitled to have the security restored or its value made good to him before, or as a condition of, the return of the payment.

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[199] For a discussion of provincial fraudulent preference legislation, see *infra*, this ch., sec. 4(a).

(5) Nothing in this Act,

(*a*) affects the *Wages Act* or prevents a debtor providing for payment of wages due by him in accordance with that Act;

(*b*) affects any payment of money to a creditor where the creditor, by reason or on account of the payment, has lost or been deprived of, or has in good faith given up, any valid security that he held for the payment of the debt so paid unless the security is restored or its value made good to the creditor;

(*c*) applies to the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors; or

(*d*) invalidates a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance in money is made to the debtor by the creditor in the *bona fide* belief that the advance will enable the debtor to continue his trade or business and to pay his debts in full.

Section 12, which deals with the tracing of proceeds, has been reproduced in an earlier portion of this chapter.[200]

(d) THE PRESENT LAW

(i) General Observations

In the course of considering fraudulent conveyances, we discussed section 4(1), a portion of section 5, and section 12 of the *Assignments and Preferences Act*. Since section 4(1) and section 4(2) are virtually identical, and since section 12 applies to actions under both provincial statutes, much of the previous discussion is relevant to fraudulent preferences.

For example, the debtor's intent to defraud one or more of his creditors is as critical to an attack on a fraudulent preference under section 4(2) as it is to an attack on a fraudulent conveyance under section 4(1).[201] In addition, both section 4(1) and section 4(2) of the *Assignments and Preferences Act* require that the impeaching creditor prove that the transaction was made by a debtor "in insolvent circumstances", or "unable to pay his debts in full", or who knows that he is "on the eve of insolvency";[202] consequently, the problems that we have noted respecting the interpretation of these phrases under section 4(1) are the same as those that arise under section 4(2). The two provisions also purport to declare the fraudulent transaction "void", although, as we have seen, the transaction is only voidable.[203] The class of persons entitled to challenge a fraudulent preference is more restrictive than the class of persons entitled to challenge a fraudulent conveyance under the *Fraudulent Conveyances Act*; the *Assignments and Preferences Act* accords the right only to "creditors", and not "creditors or others", thereby excluding, for example, persons with unliquidated claims.[204] Moreover, it appears that only creditors existing at the time of the impeached transaction can avoid it.[205] The rationale for excluding subsequent creditors from those who have standing under the preference legislation was considered in *Re Skinner*:[206]

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[200] See *supra*, at 128-29.

[201] Indeed, there is no real difference between the intent requirement under ss. 4(1) and 4(2), on the one hand, and s. 2 of the *Fraudulent Conveyances Act*, on the other: see New Brunswick Report, *supra*, note 30, at 111-12, *n*. 127, and *supra*, this ch., sec. 2(b)(iii).

[202] See *supra*, this ch., sec. 2(b)(ii).

[203] See *supra*, this ch., sec. 2(b)(i).

> I can see that in the preference cases it is only logical that if one creditor is to attack a payment to another as preferential when made then he, the attacking creditor, must also have had the status of creditor at that time. If he had not, there could be no preference, because the debt to the attacking creditor did not exist at the time. Therefore it could not be said that another creditor was preferred over him. . . .

As indicated previously, the requirement to prove that the transferee had notice or knowledge of the debtor's fraudulent intent, while explicit under the *Fraudulent Conveyances Act*, exists as a result of a judicial gloss under the *Assignments and Preferences Act*.[207] While there has been some doubt expressed as to the applicability of such a rule with respect to preference legislation, it seems that the "weight of authority greatly preponderates in favour of the view, that in order to work a fraudulent preference of a creditor under R.S.O. Ch. 118 [*The Assignments Act*, the precursor of the present *Assignments and Preferences Act*] there must be a concurrence of intent so to do on the part of both debtor and creditor".[208] Otherwise, it has been argued, the absence of such a requirement "would paralyse trade and mercantile business altogether".[209] On the other hand, at least one commentator has reacted against the rule,[210] and, in the Supreme Court of Canada, Dickson J. has cast doubts on its validity in the course of deciding a preference case in bankruptcy.[211]

(ii) The Doctrine of Pressure

The doctrine of pressure is one of long standing and provides that, where a debtor is induced to make a conveyance to a creditor because of pressure, force, demands, or requests coming from that creditor, there can be no intent to defeat remaining creditors: the motive or intent of the debtor is simply to satisfy the creditor and eliminate the pressure. A fraudulent preference, then, must be voluntarily given, at least in the absence of a statutory provision to the contrary.

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[204] See *supra*, this ch., sec. 2(b)(vi).

[205] However, the authors of the New Brunswick Report, *supra*, note 30, at 142, were not entirely convinced that the rule excluding future creditors would apply even where there was "an intention to defeat future creditors, whether generally or specifically".

[206] *Supra*, note 152, at 78.

[207] See *supra*, this ch., sec. 2(b)(v)a.(2).

[208] *Burns v. M'Kay* (1885), 10 O.R. 167 (Ch.), at 168. See *Johnson v. Hope*, *supra*, note 126, at 15-16, and *Mulcahy v. Archibald*, *supra*, note 79.

[209] *Johnson v. Hope*, *supra*, note 126, at 15.

[210] Jewers, "Fraudulent Conveyance and Preference Legislation in Canada" (1956), 28 Man. Bar News 1, at 11.

[211] See *Hudson v. Benallack*, *supra*, note 128, at 180, where Dickson J. criticized the decision in *Benallack v. Bank of B.N.A.* (1905), 36 S.C.R. 120. See, also, Dunlop, *supra*, note 39, at 539-40.

While the nature and scope of the pressure that is required to validate a transaction is by no means clear,[212] most of the cases speak in terms of pressure that impairs the debtor's spontaneity or will, thereby making it impossible to assert – at least, as a matter of law – that he had an intention to give an unjust preference. The factors involved in determining whether a preference was voluntary or made under pressure have been summarized succinctly in the New Brunswick Report to include "who originally proposed the preference, how much the creditor knows about the debtor's financial situation, to what extent the parties deal at arm's length, and the exact tone of any demand for payment made by the creditor".[213]

Conceptually, it is not difficult to understand the proposition that, where a creditor exerts pressure on a debtor to pay a debt, the debtor may not manifest any fraudulent intent in paying it. Of course, whether a particular debtor succumbs to a specific type or degree of pressure from a particular creditor may be partially dependent upon the extent to which the debtor in fact did have some desire or predisposition to give that creditor an unjust preference. Moreover, where a creditor seeks not only payment, but also an unjust preference, the transaction will be invalidated.[214] In this connection, the New Brunswick Report stated that "[p]ressure will validate the transaction even though the creditor is aware of the insolvency, and presumably aware that other creditors will be prejudiced as a result".[215] One can only speculate as to how much more would have to be shown to indicate that a creditor has sought an unjust preference.[216]

Aside from the fact that the doctrine of pressure seems to breed rather arid arguments concerning the debtor's and creditor's true intent or motives, the application of the doctrine permits an insensitive or very active creditor to reap the benefits of his harassment of the debtor, unless of course he oversteps that barely visible line and seeks an "unjust preference". In addition, the doctrine arguably flies in the face of the *Assignments and Preferences Act*, which is designed to prohibit preferences under circumstances where an equal division of assets is thought to be desirable.

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[212] In *Re Carson*, [1924] 55 O.L.R. 649, 4 D.L.R. 492, 4 C.B.R. 683 (App. Div.), Orde J.A. stated that pressure must involve the threat or belief that legal proceedings will be instituted. In *The Molson Bank v. Halter* (1890), 18 S.C.R. 88, Strong J. said that a mere demand was sufficient. See, also, *Stephens v. McArthur*, *supra*, note 128.

[213] New Brunswick Report, *supra*, note 30, at 123, *n*. 160.

[214] *Powell v. Calder* (1885), 8 O.R. 505 (Ch.).

[215] New Brunswick Report, *supra*, note 30, at 123. The Report cited *W.G. Craig & Co. v. Gillespie* (1920), 47 O.L.R. 529, 54 D.L.R. 514 (H.C. Div.), and *Brown v. Bank of Montreal* (1916), 23 B.C.R. 68 (C.A.).

[216] The New Brunswick Report did acknowledge the difficulty (*supra*, note 30, at 123-24): "Obviously, the dividing line between these . . . rules is difficult to draw, just as is the dividing line between mere notice of intent to defeat creditors and privity to such intent."

(iii) Statutory Presumptions

A significant formal difference between the *Assignments and Preferences Act* and the *Fraudulent Conveyances Act* is the existence of a statutory, as opposed to court-developed, *prima facie* presumption of fraudulent intent. This presumption, contained in section 4(3) of the former Act, arises where the transaction "has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them" and where the action to impeach it is brought within sixty days of the transaction. It will be recalled that the courts have been rather liberal in using inferences and presumptions when the *Fraudulent Conveyances Act* has been invoked; for example, the now generally prevailing view is that there is a rebuttable presumption of fraudulent intent where the effect of a conveyance is to defeat creditors.[217] In this sense, then, section 4(3) of the *Assignments and Preferences Act* is unique only in that it makes explicit a presumption that has led to a considerable degree of confusion under 13 Eliz., c. 5, and its Ontario counterpart.

In practice, a significant number of preferences are challenged within the sixty day impeachment period. In fact, many solicitors appear to be of the view that it is only the existence of the section 4(3) presumption that assures them of any hope of success. This perception, however, may be somewhat myopic in light of the inferences and presumptions ordinarily marshalled in *Fraudulent Conveyances Act* proceedings, which are analogous, and, more recently, in preference cases in which the statutory presumption is not applicable. In the latter connection, reference should be made, for example, to the Nova Scotia case of *West v. Avco Financial Services Canada Ltd.*,[218] where the Court dealt with the burden of proof in an action brought outside the sixty day period. Cooper J.A. stated as follows:[219]

> I address myself first to the burden of proof which rested upon Avco as the plaintiff in the action. I respectfully adopt what was said by Chief Justice Cowan of the Trial Division of this Court in *Royal Bank of Canada v. Kirkpatrick et al.* (1975), 20 N.S.R. (2d) 458 at p. 468:
>
>> With regard to the burden of proof that the transfer of the property in question was made with intent to defeat, hinder, delay or prejudice the plaintiff creditor, it is clear that, if the effect of the transfer might be expected to be, and has, in fact, been to defeat, hinder, delay, or prejudice the creditor, the Court will attribute the fraudulent intention to the settlor.

Since the debtor will normally be insolvent or unable to pay his debts generally in a preference action, the transaction will ordinarily have the effect mentioned above, in which case the evidentiary burden will be placed on the debtor – a shift accomplished within the sixty day period by the statutory presumption. This rather unorthodox view – a view that is reminiscent of the now largely discredited *Freeman v. Pope* doctrine in the context of fraudulent conveyances – would, therefore, result in the elimination of any real distinction between preference actions brought within, and those brought outside, the sixty day period.

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[217] See *supra*, this ch., sec. 2(b)(iii)b.

[218] (1979), 101 D.L.R. (3d) 83 (N.S.S.C., App. Div.).

[219] *Ibid.*, at 84-85. A similar view was expressed in *Wilson Equipment Ltd. v. Union Construction Ltd.* (1979), 31 C.B.R. (N.S.) 208 (N.S.S.C.).

Finally, it should be noted that, under section 4(3), the doctrine of pressure is expressly abrogated. Accordingly, a preferred creditor ostensibly cannot rely simply on proof that he wished only to collect his debt.

(iv) Protected Transactions

When considering fraudulent conveyances under section 4(1) of the *Assignments and Preferences Act*, we had occasion to discuss certain transactions protected under that statute.[220] We therefore have considered, and need not discuss further, a number of matters that are relevant in the fraudulent preference context as well, such as the insolvency prerequisite in section 4(1), the judicially created concurrent intent doctrine, and the proviso respecting "fair and reasonable" consideration in section 5(1).[221] In the sections that follow, it is intended to discuss other saving provisions, contained in section 5 of the Act, that relate to preferences.

a. "Any Payment of Money to a Creditor"

One protective provision, which does not appear to involve any requirement of *bona fides*, is the provision in section 5(1) excepting from section 4(2) "any payment of money to a creditor". If the section 5(1) proviso concerning "fair and reasonable" consideration modifies this provision, then the latter would not seem to be particularly controversial, although, to the extent that the exception was intended to facilitate the payment of ordinary trade debts in the normal course of business, it appears to be redundant: section 5(1) already contains an exception for any "payment made in the ordinary course of trade or calling to an innocent . . . person". However, it bears emphasizing that the latter exception requires the payment to be "*bona fide*".

While the above interpretation of the exception for "any payment of money to a creditor" seems to be reasonable, notwithstanding the duplication described in the preceding paragraph, it has been suggested that the protective provision may in fact be read independently of the "fair and reasonable" consideration proviso.[222] If so, then the provision is a startling one indeed, since it effectively legitimizes the most common type of preference – the payment of money to a creditor in respect of an antecedent debt – and flies in the face of the very purpose of the *Assignments and*

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[220] See *supra*, this ch., sec. 2(b)(v).

[221] See *Leighton v. Muir*, *supra*, note 84. See *supra*, this ch., sec. 2(b)(v)b.(1), with respect to this case.

[222] See New Brunswick Report, *supra*, note 30, at 129, *n*. 173.

Preferences Act. The bizarre nature of this interpretation is made even clearer when one reflects on the apparent absence of any good faith requirement respecting the debtor's payment to his creditor.

Even assuming a satisfactory explanation for the adoption of this exception, there are difficulties with the manner in which the provision has been interpreted. While a payment by cheque drawn by the debtor and payable to the preferred creditor comes within the purview of this exception, it would appear that certain other types of payment do not.[223]

b. A "Bona Fide . . . Payment Made in the Ordinary Course of Trade or Calling"

Another exception, contained in section 5(1), provides that nothing in section 4 applies to "any *bona fide* . . . payment made in the ordinary course of trade or calling to an innocent . . . person". To the extent that this exception comprehends payments to a creditor in respect of an antecedent debt, it appears to be redundant, at least in part, in light of the exception for "any payment of money to a creditor".

c. Transactions Made in Consideration of a "Present Actual Bona Fide . . . Delivery of Goods or Other Property"

Section 5(1) contains an exception for "any *bona fide* conveyance, assignment, transfer or delivery over of any goods or property of any kind that is made in consideration of a present actual *bona fide* . . . delivery of goods or other property". This saving clause overlaps somewhat with the exception, discussed above, for any "*bona fide* . . . payment made in the ordinary course of trade or calling", but is wider than the latter exception. For example, it would appear to comprehend a transaction with a creditor by a debtor not engaged in any "trade or calling".

d. Security Given to a Creditor

Sections 5(1), 5(4), 5(5)(*b*), 5(5)(*c*), and 5(5)(*d*) of the *Assignments and Preferences Act* contain exceptions to section 4(2) in respect of security given by a debtor to his creditor. We shall deal with these exceptions below.

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[223] *Ibid.*, at 130-31 (footnote references omitted):

> [T]he endorsement to the creditor of a cheque payable to the debtor is not a payment of cash unless, it would appear, the creditor is the debtor's bank. A transaction in which the debtor transfers property to a third party in consideration in whole or part of a cash payment by the third party to a creditor is regarded as a payment of cash. On the other hand, a transaction in which goods are sold by the debtor to a creditor in return for cash which is immediately handed over in payment of the creditor's claim is not regarded as a true payment of cash.

See, also, *ibid.*, at 130, *n*. 176.

(1) *Voidable Payments under Sections 5(4) and 5(5)(b)*[224]

Section 5(5)(*b*) provides that nothing in the Act affects "any payment of money" to a creditor where the creditor, "by reason or on account of the payment, has lost or been deprived of, or has in good faith given up" any security he held for repayment, unless the security is restored or its value made good to the creditor; if the security is restored or its value made good, the payment of money may be declared void. Section 5(4) provides for the same result, although from a different perspective. This section deals with a situation where a "payment" made to a creditor is invalid and where the secured party gave up his security in consideration of the payment, and provides that "the creditor is entitled to have the security restored or its value made good to him before, or as a condition of, the return of the payment".

In addition to the duplication between section 5(4) and section 5(5)(*b*), there appears to be some overlap between these two provisions and the broad exception in section 5(1) that provides that nothing in section 4 applies to "any payment of money to a creditor". This latter provision, considered earlier, would seem to exempt *all* payments of money to creditors in respect of an antecedent debt, regardless of whether the creditor in question gives up any security held by him.[225]

(2) *Substitution of One Security for Another*

Section 5(5)(*c*) of the *Assignments and Preferences Act* provides that nothing in the Act "applies to the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors. . .". This exception, which reflects a common commercial practice, seems both innocuous and reasonable.

(3) *Security for a Pre-Existing Debt Accompanied by a Present Advance*

Section 5(5)(*d*) provides for an exception to section 4(2) where security is given for an antecedent debt, if accompanied by a present advance. The section provides that nothing in the Act "invalidates a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance in money is made to the debtor by the creditor in the *bona fide* belief that the advance will enable the debtor to continue his trade or business and to pay his debts in full".

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[224] Section 5(5)(*b*) is the direct lineal descendant, in somewhat amended form, of a portion of s. 3(2) of *An Act respecting Assignments for the Benefit of Creditors*, 48 Vict., c. 26 (see *supra*, note 20, and supporting text), that was added in 1886 to the Act by s. 1 of *An Act to Amend the Act Respecting Assignments for the Benefit of Creditors*, 49 Vict., c. 25. Section 5(4) was added in 1887 as s. 2a of that statute by *An Act to make further provisions respecting Assignments for the Benefit of Creditors*, 50 Vict., c. 19, s. 3, in part.

[225] Since s. 5(4), unlike s. 5(5)(*b*), does not refer to the "payment of money" but only to "payment", it may be thought that the former was intended to be more comprehensive, including payment in kind. However, is it reasonable to assume that special provision would be made for the relatively infrequent case in which a debtor repays his creditor in property rather than cash or cheque?

It should be borne in mind that, while the security given by the debtor ordinarily would bear a fair value relative to the pre-existing debt, the advance could be far less than the value of the security. This fact is important when one bears in mind that in no other circumstance can a debtor give a preference by way of security for a pre-existing debt. Under section 5(5)(*d*), then, the remaining creditors could be deprived of a valuable asset in exchange for which the debtor could receive a relatively insignificant amount, perhaps in furtherance of a very speculative venture, or even a fraud. Presumably, however, the Legislature was of the view that this exception was commercially essential; if the debtor was successful in continuing his business, theoretically all creditors would reap the benefit. Of course, since by definition the advance is to be employed in resurrecting a financially troubled enterprise, the risk is correspondingly greater. In some cases, it might even be financially preferable to let the business collapse and save the valuable asset for execution and sale for the benefit of all creditors. Unfortunately, there is no way of stating a categorical rule that would help to assess the merits or consequences of section 5(5)(*d*) as a general matter.

It also should be pointed out that, even in the absence of section 5(5)(*d*), the creditor's "*bona fide* belief that the advance will enable the debtor to continue his trade or business and to pay his debts in full" might well be sufficient to negative a concurrent fraudulent intent on his part.[226] Consequently, it is likely that the transaction would be saved in any event. Again, it is not improbable that the section was introduced to put the matter beyond all peradventure.

(4) *"Security for a Present Actual Bona Fide Advance of Money"*

Section 5(1) of the *Assignments and Preferences Act* provides, *inter alia*, that nothing in section 4(2) applies to "any *bona fide* conveyance, assignment, transfer or delivery over of any goods or property of any kind . . . by way of security for a present actual *bona fide* advance of money". This saving provision is subject to the proviso that "the goods or other property . . . delivered [must] bear a fair and reasonable relative value to the consideration therefor" – that is, in this case, to the "advance of money". Theoretically, then, the value of the debtor's estate would not have been altered by the transaction.

(5) *An Agreement to Give Security at Some Future Date*

In *River Stave Co. v. Sill*,[227] it was stated by way of *obiter dicta* that an agreement entered into prior to insolvency, whereby the debtor agrees to give security at some time in the future, would not validate a security given after insolvency and later challenged under the Act. Armour J. stated that the security, not given for a "present actual *bona fide* advance of money", did not come within the purview of what is now section 5(1), and that the security, not taken in the *bona fide* belief that the advance would assist the debtor in his business, did not come within present section 5(5)(*d*).[228] However, in *McCurdy v. Grant*,[229] the Court arrived at the opposite conclusion, although again by way of *obiter dicta*. In addition, under the preference legislation in the *Bankruptcy Act*,[230] it has been held that a prior agreement rebuts an intention to give an unjust preference.[231]

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[226] For an analogous case involving the rebuttal of the presumption of the debtor's intent, see *Re K. & C. Thermoglass Ltd.* (1979), 16 B.C.L.R. 33, 32 C.B.R. (N.S.) 166 (S.C.).

[227] *Supra*, note 198.

e. Payment Pursuant to Another Statute

Section 5(5)(*a*) provides that nothing in the *Assignments and Preferences Act* "affects the *Wages Act*[232] or prevents a debtor providing for payment of wages due by him in accordance with that Act". In considering the comparable provision in New Brunswick, the New Brunswick Report stated that, "[s]ince such payments are required by law, it is doubtful that they could be said to be unjust preferences in any event".[233] However, the Report was of the view that all priorities "to which a creditor is entitled by law" should receive the same explicit treatment,[234] presumably if only out of an abundance of caution.

4. FRAUDULENT CONVEYANCES AND PREFERENCES IN OTHER JURISDICTIONS

(a) PROVINCIAL LEGISLATION IN CANADA

Fraudulent conveyance legislation comparable to the Ontario *Fraudulent Conveyances Act* has been enacted in British Columbia, Manitoba and Newfoundland. In Quebec, fraudulent conveyance and fraudulent preference legislation appears in the *Civil Code*. In other provinces, 13 Eliz., c. 5, remains part of the general law, and in all common law provinces, except Newfoundland, a fraudulent conveyance provision akin to section 4(1) of the Ontario *Assignments and Preferences Act* appears in the statutes dealing mainly with preferences. Since 13 Eliz., c. 5, is the precursor of the modern enactments, the operation of the law of fraudulent conveyances in the provinces in which it is in force essentially parallels that in the provinces with statutes akin to our *Fraudulent Conveyances Act*. For this reason, we make only brief reference to fraudulent conveyances in the following discussion.

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[228] *Ibid.*, at 569-70.

[229] (1900), 32 N.S.R. 520 (C.A.).

[230] R.S.C. 1970, c. B-3.

[231] *Re Shaugnessy Super Market and Codville Co. Ltd.* (1963), 37 D.L.R. (2d) 524 (Man. Q.B. in Bktcy.). The bankruptcy provisions are described *infra*, this ch., sec. 4(b).

[232] R.S.O. 1980, c. 526.

[233] New Brunswick Report, *supra*, note 30, at 134.

[234] *Ibid.*, at 134, *n.* 183.

Greater differences emerge, however, in a comparison of the statutes governing preferential transactions. In Canada, preference legislation has been enacted in all provinces except Newfoundland.

(i) Newfoundland

While there are no statutory provisions in Newfoundland respecting preferential transactions, the Legislature recently adopted *The Fraudulent Conveyances Act*.[235] The only difference in the wording between the Newfoundland statute and the Ontario *Fraudulent Conveyances Act* is contained in section 2(a) of the former, which defines "conveyance" to include "transfer, assignment, delivery over, payment, gift, grant, alienation, bargain, charge, incumbrance, limitation of use or uses of, in, to or out of real property or personal property by writing or otherwise". The corresponding definition in the Ontario *Fraudulent Conveyances Act* omits the words "transfer, assignment, delivery over, payment", although section 4(1) of the Ontario *Assignments and Preferences Act* refers to "every gift, conveyance, assignment or transfer, delivery over or payment". There appears to be no case law on point, and one can only conjecture that these words were added for greater comprehensiveness.

(ii) Prince Edward Island

In Prince Edward Island, fraudulent conveyances are governed by 13 Eliz., c. 5. In addition, the Legislature has adopted the *Frauds on Creditors Act*,[236] which covers basically the same ground as sections 3 to 5 of the Ontario *Assignments and Preferences Act*. With respect to preferences, there is considerable similarity, but some differences, between the Ontario and Prince Edward Island statutes. For example, whereas section 4(2) of the Ontario Act implicitly retains the doctrine of pressure generally in preference actions, under section 2(2) of the *Frauds on Creditors Act*, comparable to section 4(2), the doctrine of pressure is abrogated for all preference transactions voidable under the Act.[237]

Another radical departure from Ontario law is to be found in section 2(5) of the Prince Edward Island legislation, which provides that "[t]he intent referred to in this section and in section 1[238] is the intent of the assignor or transferor, and no concurrence therein, or knowledge thereof, or of insolvency, need be shown in the assignee or transferee". By the abrogation of the doctrine of pressure and of the need to prove concurrent intent, the Prince Edward Island Act is closer than the Ontario Act to the policy of ensuring that all creditors of an insolvent debtor-transferor are dealt with equally. The shift is away from emphasis on the fraudulent intent of the transferee and even, having regard to the inapplicability of the doctrine of pressure, that of the debtor.

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[235] S.N. 1974, No. 29. There are no corresponding provisions in the Newfoundland Act to ss. 5-8 of the Ontario *Fraudulent Conveyances Act*, dealing with conveyances in fraud of purchasers.

[236] R.S.P.E.I. 1974, c. F-13. This statute does not provide for assignments for the benefit of creditors. The opening words of s. 3(1) provide that "[n]othing in the preceding section applies to any authorized assignment made under the *Bankruptcy Act* (Canada) R.S.C. 1970, Chap. B-3".

[237] In addition to the general abrogation of the doctrine of pressure in s. 2(2) of the *Frauds on Creditors Act*, the Act contains a provision – s. 2(3) – virtually identical to Ontario s. 4(3), which makes the doctrine inapplicable during the special 60 day impeachment period.

[238] Section 2 corresponds to s. 4, and s. 1 corresponds to s. 3, of the Ontario *Assignments and Preferences Act*.

(iii) Nova Scotia and New Brunswick

The Statute of Elizabeth is in force in both Nova Scotia[239] and New Brunswick.[240] For voiding preferential transactions by insolvents, the provisions of the *Assignments and Preferences Acts*[241] are available. These Acts are basically the same as their Ontario counterpart.

(iv) Quebec

The provisions dealing with fraudulent conveyances and preferences are to be found in articles 1032 - 1040 of the *Civil Code*. Article 1032 states the general principle that "[c]reditors may in their own name impeach the acts of their debtors in fraud of their rights, according to the rules provided in this section". Article 1033 establishes two conditions for the voiding of a fraudulent contract, providing that "[a] contract cannot be avoided unless it is made by the debtor with intent to defraud, and will have the effect of injuring the creditor".

Where insolvency is involved, the *Civil Code* provides a statutory presumption of fraudulent intent in three instances. Articles 1034 and 1035 deal with fraudulent contracts, while article 1036 concerns fraudulent preferences:

> 1034. A gratuitous contract is deemed to be made with intent to defraud, if the debtor be insolvent at the time of making it.
>
> 1035. An onerous contract[242] made by an insolvent debtor with a person who knows him to be insolvent is deemed to be made with intent to defraud.
>
> 1036. Every payment by an insolvent debtor to a creditor knowing his insolvency, is deemed to be made with intent to defraud, and the creditor may be compelled to restore the amount or thing received or the value thereof, for the benefit of the creditors according to their respective rights.

These three presumptions, which are rebuttable,[243] are not dissimilar to the presumptions developed by Ontario courts.

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[239] See *Leighton v. Muir*, *supra*, note 84; *Cromwell v. Comeau*, *supra*, note 83; and *Bank of Montreal v. Crowell*, *supra*, note 24.

[240] See, for example, *Bank of Montreal v. Vandine*, *supra*, note 45, and *Can. Pittsburgh Industries Ltd. v. Sherman Hardware Ltd.* (1970), 2 N.B.R. (2d) 264 (S.C., T.D.).

[241] R.S.N.S. 1967, c. 16, and R.S.N.B. 1973, c. A-16. These statutes also contain a provision – in ss. 3(1)(a) and 2(1), respectively – akin to s. 4(1) of the Ontario *Assignments and Preferences Act*.

[242] An "onerous contract" is one in which consideration has been given.

[243] See, for example, *In Re Normandin (Debtor): Inns v. Dominion Structural Steel Ltd.*, [1959] B.R. 14, with respect to art. 1036.

The combined effect of articles 1033 and 1034 is worth mentioning. Where an insolvent debtor enters into a gratuitous contract, the intent to defraud requirement imposed by article 1033 will be satisfied as a result of the presumption in article 1034, and, by definition, so will the prejudicial effect requirement, since a gratuitous contract by an insolvent debtor will inevitably defeat creditors. In other words, the two provisions create a regime in which a transaction can be set aside where it has the effect of injuring creditors.

It will be noted that the state of mind of the creditor that is required to be shown under articles 1035 and 1036 is only that he knows the debtor to be insolvent – not that he is somehow "privy" to the debtor's fraud, as may be required in analogous circumstances in Ontario.[244] With respect to the transferee's intent, reference also should be made to article 1038, which provides that "[a]n onerous contract made with intent to defraud on the part of the debtor, but in good faith on the part of the person with whom he contracts is not voidable; saving the special provisions applicable in case of insolvency of traders". Presumably, then, mere knowledge of insolvency will not preclude an "onerous contract" from being upheld, so long as the transferee acts "in good faith". However, no such similar dispensation appears to be granted to a good faith transferee under a "gratuitous contract".

(v) Manitoba, Saskatchewan, Alberta, and British Columbia

The law respecting fraudulent conveyances in these four jurisdictions generally mirrors that in Ontario.[245] Consequently, attention will be focused on the various fraudulent preferences Acts, using the Manitoba legislation as an illustration. The provisions relating to preferences are contained in sections 39 to 47 and 49(1) of the Manitoba *Assignments Act*.[246] Section 39 and sections 44 to 47 correspond, respectively, to section 4(1) and section 5 of the Ontario *Assignments and Preferences Act*. For our purpose, attention should be drawn to sections 40 and 42 of the Manitoba Act, for, read together, they contain certain features not found in the Ontario legislation. Sections 40 and 42 read as follows:

> 40. Subject to sections 44 to 47, every such gift, conveyance, assignment, or transfer, delivery over or payment as aforesaid, made to or for a creditor by a person at any time when he is in insolvent circumstances, or is unable to pay

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[244] See *supra*, this ch., secs. 2(b)(iv)c. and 2(b)(v)a.(2).

[245] In Manitoba, see *The Fraudulent Conveyances Act*, R.S.M. 1970, c. F160, and in British Columbia, see *Fraudulent Conveyance Act*, R.S.B.C. 1979, c. 142. In Alberta and Saskatchewan, 13 Eliz., c. 5, applies.

The Manitoba *Fraudulent Conveyances Act* does contain an expanded definition of "conveyance" to include "transfer, assignment, delivery over, payment" – akin to the definition of "conveyance" in Newfoundland's *Fraudulent Conveyances Act*, S.N. 1974, No. 29, s. 2(a), reproduced *supra*, this ch., sec. 4(a)(i) – and a saving provision with respect to conveyances by tenants in tail.

[246] R.S.M. 1970, c. A150. This statute also contains a provision – s. 38 – akin to s. 4(1) of the Ontario *Assignments and Preferences Act*, as does the *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18 (s. 3(a)), the *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143 (s. 3(a)), and *The Fraudulent Preferences Act*, R.S.S. 1978, c. F-21 (s. 3).

> his debts in full, or knows that he is on the eve of insolvency, and that has the effect of giving that creditor a preference over the other creditors of the debtor, or over one or more of them, is void, in and with respect to any action or proceeding that, within sixty days thereafter, is brought, had, or taken, to impeach or set aside the transaction, and as against the creditor or creditors injured, delayed, prejudiced, or postponed.
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> 42.-(1) A transaction shall be deemed to be one that has the effect of giving a creditor a preference over other creditors within the meaning of [section] 40 . . . if by the transaction a creditor is given, or realizes, or is placed in a position to realize, payment, satisfaction or security for the debtor's indebtedness to him, or a portion thereof, greater proportionately than could be realized by or for the unsecured creditors generally of the debtor, or for the unsecured portion of his liabilities, out of the assets of the debtor left available and subject to judgment, execution, attachment, or other process.
>
> (2) That effect shall not be deemed dependent upon the intent or motive of the debtor or upon the transaction being entered into voluntarily or under pressure.
>
> (3) No pressure by a creditor, or want of notice to the creditor alleged to have been so preferred of the debtor's circumstances, inability, or knowledge as aforesaid, or of the effect of the transaction, avails to protect the transaction, except as provided by sections 44 and 47.

It should be noted that section 40 provides that a preferential transaction that has the effect of giving a creditor a preference and is impeached within sixty days of its execution is "void". This language should be compared to its counterpart, section 4(3) of the Ontario *Assignments and Preferences Act*, which provides that, within the sixty day period, preferential transactions shall "be presumed *prima facie* to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act". The presumption in the Ontario Act is clearly rebuttable, so that evidence of the debtor's actual intent would be admissible. However, in Manitoba, under section 40, successful avoidance of the transaction is dependent solely upon its preferential "effect", and section 42(2) makes it clear that the "effect" to which reference is made has nothing to do with the "intent or motive" of the debtor.[247] Consequently, even if the debtor had no fraudulent intent whatsoever, and acted solely under pressure from the preferred creditor, sections 40 and 42 presumably could be invoked to avoid the transaction within sixty days of its execution.

Insofar as preference legislation in British Columbia, Alberta, and Saskatchewan is concerned, with regard to actions brought within the relevant impeachment period,[248] and subject to certain exceptions, there seems to be an irrebuttable presumption of invalidity where the debtor is in insolvent circumstances, unable to pay his debts in full, or knows that he is on the eve of insolvency, and where the transaction has the effect of giving a creditor a preference over other creditors.[249] Similarly, each Act has its equivalent of section 42 of the Manitoba *Assignments Act* with respect, for example, to the immateriality of the debtor's intent and the abrogation of both the doctrine of pressure and the requirement of concurrent intent.[250] As a result of such provisions, there exists in these provinces a regime in which a transaction may be impeached because of its prejudicial effect, at least within the statutory impeachment period. Neither the debtor's intent or motive, nor the preferred creditor's pressure or want of knowledge, can have any legitimizing influence. Consequently, it may be said that these provisions lean more heavily toward a policy of creditor protection and equality than do those in Ontario.

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[247] Why s. 42(2) is worded so that the prejudicial "effect" of a transaction – an objective phenomenon – is said not to be deemed to be dependent upon the subjective factors of intent or motive is unclear; the legislation could have provided simply that the debtor's intent is immaterial in the 60 day period.

[248] The impeachment period is 1 year in Alberta and 60 days in British Columbia and Saskatchewan.

(vi) Conclusion

With respect to fraudulent conveyances legislation, it need only be said that there is much uniformity across Canada. However, it is clear from a brief survey of provincial fraudulent preferences law that, despite what appears to be the similar purpose of the various statutes, there are some significant differences. The critical issue is the extent to which the preference legislation promotes the protection of all creditors and maintains an even distribution of a debtor's assets among them. On the one hand, the Ontario *Assignments and Preferences Act* focuses on fraudulent intent; even within the sixty day impeachment period, while the doctrine of pressure has been abolished, the statutory presumption of fraudulent intent is rebuttable. On the other hand, the Prince Edward Island *Frauds on Creditors Act* abrogates the doctrine of pressure for all transactions, not merely those brought within sixty days of the execution of the transaction.[251] Moreover, section 2(5) provides that the intent referred to in section 2, whether within the impeachment period or not, is the debtor's intent "and no concurrence therein, or knowledge thereof, or of insolvency, need be shown in the . . . transferee". Accordingly, the Prince Edward Island statute has moved some distance in furthering the equal distribution philosophy inherent in creditors' relief legislation. The only caveat is that the above section is subject to a saving provision like section 5 of the Ontario *Assignments and Preferences Act*.

The Western provinces have effected a compromise between furthering the rateable distribution philosophy by avoiding all prejudicial preferences by insolvent debtors, and permitting every debtor to pay his creditors as he sees fit. These provinces have provided that, within the special statutory impeachment period, the sole criterion for avoiding the transaction is its prejudicial effect as a preference. The legislation illustrates that a type of regime that avoids all prejudicial preferential transactions, either generally or within a stipulated period of time, irrespective of the intent of the debtor or transferee, is not universally regarded as philosophically unsound or impracticable.

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[249] See *Fraudulent Preferences Act*, R.S.B.C. 1979, c. 143, s. 4; *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18, s. 3; and *The Fraudulent Preferences Act*, R.S.S. 1978, c. F-21, s. 5.

[250] See s. 5 of the British Columbia Act, s. 4(2) of the Alberta Act, and s. 6 of the Saskatchewan Act.

[251] See *supra*, note 236, s. 2(1), (2) and (3).

(b) Bankruptcy Legislation in Canada

(i) Introduction

"It is a prime requirement of bankruptcy legislation that it permit a thorough investigation of fraudulent transactions and provide effective remedies for dealing with them."[252] This portion of the chapter will examine the provisions of the *Bankruptcy Act*[253] and Bill C-12,[254] the proposed new bankruptcy legislation, relating to the avoidance of fraudulent transactions.

However, before focusing attention on bankruptcy legislation, reference should be made to the applicability of provincial law. Despite some earlier case law to the contrary, it would appear that, in bankruptcy proceedings, fraudulent preferences may be attacked under section 4(2) of the *Assignments and Preferences Act*. In the recent case of *Robinson v. Countrywide Factors Ltd.*,[255] the Supreme Court of Canada considered the right of the trustee in bankruptcy to use the Saskatchewan *Fraudulent Preferences Act*[256] to set aside transactions of the bankrupt. Spence J., for the majority, held that the provincial legislation was *intra vires*, and that sections 3 and 4 were not in conflict with the *Bankruptcy Act*. The Parliament of Canada had refrained from covering completely the whole field of transactions avoided by provincial legislation. Mr. Justice Spence found support for his conclusion in section 50(6) of the *Bankruptcy Act*, which provides for the utilization of provincial laws "relating to property and civil rights that are not in conflict with this Act".[257] Mr. Justice Beetz noted that other provincial statutes found to be *ultra vires* were predicated upon insolvency and set up an elaborate, comprehensive scheme regulating the distribution of a debtor's assets among all his creditors. No such system, he said, was established under the Saskatchewan Act.

Laskin C.J. dissented. Essentially, he based his conclusion on the ground that insolvency was the *sine qua non* of impeachability under the Act and, therefore, a direct invasion of the exclusive federal jurisdiction in relation to "insolvency". It bears mentioning, however, that Chief Justice Laskin was careful to limit the scope of his dissent to the provisions of the Saskatchewan *Fraudulent Preferences Act* (and, clearly, other similar provincial Acts). He stated that nothing in his judgment was intended to raise doubts concerning the validity of such statutes as the Ontario *Fraudulent Conveyances Act*, which, he noted, do not require proof of insolvency.

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[252] Houlden, "Bankruptcy Legislation" (1965), 7 C.B.R. (N.S.) 217, at 225.

[253] *Supra*, note 7.

[254] *Supra*, note 8.

[255] [1978] 1 S.C.R. 753, (1977), 72 D.L.R. (3d) 500, 2 W.W.R. 111, 23 C.B.R. (N.S.) 97 (S.C.C.), applied in *Re Hansen* (1977), 26 C.B.R. (N.S.) 57 (Ont. S.C. in Bktcy.); *Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd.* (1977), 4 Alta. L.R. (2d) 319, 25 C.B.R. (N.S.) 207 (S.C., T.D.); and *Federal Business Development Bank v. Van Klaveren*, *supra*, note 24.

[256] R.S.S. 1965, c. 397.

[257] However, s. 10(3) of Bill C-12, *supra*, note 8, is unambiguous in its exclusion of provincial fraudulent preference and conveyance legislation in the bankruptcy context.

Under Bill C-12, section 10(2) provides for the retention of otherwise valid provincial legislation not in conflict with the new Act. Section 10(3), however, eliminates the right of trustees to use provincial voidable transactions legislation; this does not, of course, mean that such legislation, if valid, cannot be employed in a non-bankruptcy context. Since, as a very general proposition, the bankruptcy scheme in Bill C-12 differs little from the present *Bankruptcy Act*, we believe that the adoption of Bill C-12 would have no effect on the constitutionality of existing provincial law, nor, in view of the nature of our proposals in this chapter, on the regime that we shall recommend below.

(ii) Fraudulent Preferences

a. General Scheme of Existing and Proposed Legislation

Sections 73 and 74 of the *Bankruptcy Act*, the central provisions that declare certain preferences[258] void, are a means of carrying into effect the general bankruptcy principle that all ordinary, unsecured creditors should rank equally. These provisions read as follows:

> 73.-(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.
>
> (3) For the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor.
>
> 74. Where the conveyance, transfer, charge, payment, obligation or judicial proceeding mentioned in section 73 is in favour of a person related to the in-

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[258] The term "preference" is not defined in the *Bankruptcy Act*. It is defined in s. 2(1) of Bill C-12, *supra*, note 8, to mean "a transfer made or allowed by a debtor to, or for the benefit of, a creditor for or on account of an antecedent debt, the effect of which transfer is to allow the creditor to receive in the aggregate a greater percentage of that debt than the other creditors entitled to the same or higher priority would receive if such transfer had not been made or allowed".

> solvent person, the period limited in subsection 73(1) shall be twelve months instead of three months.

Under sections 73 and 74, then, there are three conditions that must be established by the trustee in bankruptcy in order to set aside a fraudulent preference: (a) the transaction must have taken place within three months of bankruptcy or within twelve months where the insolvent person and the preferred creditor are "related";[259] (b) the debtor must have been insolvent at the date of the alleged preference; and (c) the transaction must have been made with a view to giving the creditor a preference over other creditors. If the trustee succeeds in establishing the first two elements and, in addition, shows that the effect of the impugned transaction was to give preferential treatment to the creditor who received it,[260] there arises under section 73(2) a *prima facie* presumption that it was made with a view to giving a preference, whether it was made voluntarily or under pressure.

Sections 172, 173, and 175(1) of Bill C-12 deal with fraudulent preferences in the following manner:

> 172. The court, on application of the trustee, may set aside a transfer that is a preference in favour of a creditor at arm's length with the debtor where
>
> (*a*) the transfer was made less than three months before the date of filing of a petition;
>
> (*b*) the debtor was insolvent at the time of the transfer; and
>
> (*c*) the transfer was made with the intent of the debtor to give a preference.
>
> 173.-(1) The court, on application of the trustee, may set aside a transfer that is a preference in favour of a creditor who is not at arm's length with the debtor where it is proved that
>
> (*a*) the transfer was made less than three years before the date of filing of a petition;
>
> (*b*) the debtor was insolvent at the time of the transfer; and
>
> (*c*) the transfer was made with the intent of the debtor to give a preference.
>
> (2) For the purposes of subsection (1), a transfer to a creditor made more than forty-five days and less than one year before the filing of the petition is deemed to have been made with the intent of the debtor to give a preference unless the creditor proves that the transfer was made in the normal course of affairs of the debtor in relation to the creditor.

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[259] See *Bankruptcy Act*, *supra*, note 7, s. 4, respecting "related" persons.

[260] It must be shown that the effect of the transfer was to give preferential treatment at the date when it was made, not at the date of bankruptcy: see *Re Van Der Liek* (1970), 14 C.B.R. (N.S.) 229 (Ont. S.C. in Bktcy.), at 231.

> (3) For the purposes of subsection (1), a transfer to a creditor made less than forty-five days prior to the date of filing of the petition is deemed to have been made with the intent of the debtor to give a preference unless the creditor proves that the transfer was made
>
> (*a*) in the normal course of affairs of the debtor in relation to the creditor; and
>
> (*b*) in satisfaction of a debt incurred within thirty days of the transfer.
>
> 175.-(1) Where the court, pursuant to this Part, sets aside a transfer, the court may make an order
>
> (*a*) empowering the trustee to recover the property or the value thereof from the person to whom the bankrupt transferred the property or, subject to subsection (2), from any other person to whom the property has been transferred;
>
> (*b*) assigning to the trustee the rights of the creditor in property subject to a security interest that is set aside pursuant to this Part;
>
> (*c*) subrogating the trustee to the rights of the transferor to compel payment or satisfaction where the consideration payable for or on a transfer of property or any part thereof remains unsatisfied;
>
> (*d*) restoring in so far as possible each party to the transfer to the state that he was in immediately prior to the making of the transfer; or
>
> (*e*) vesting in the trustee any rights or powers required by the trustee for the benefit of the estate.

There are, then, certain differences between Bill C-12 and the *Bankruptcy Act*. For example, unlike the situation under the present Act, Bill C-12 contains no presumption of intent in the case of arm's length transactions.[261]

b. Insolvency

As was noted above, under sections 73 and 74 of the *Bankruptcy Act* the trustee must show that the debtor was insolvent at the date of the alleged fraudulent preference. An "insolvent person" is defined in section 2 of the Act as follows:

> 2. In this Act . . .
>
> 'insolvent person' means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

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[261] It will be recalled that, under s. 73(2) of the *Bankruptcy Act*, a presumption of intent arises where the effect of the transaction is to give a preference, whether or not the parties are related.

> (*a*) who is for any reason unable to meet his obligations as they generally become due, or
>
> (*b*) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (*c*) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; . . .

These three tests of insolvency are stated disjunctively and it is not necessary for the trustee to prove more than one of them.[262]

Insolvency must be established by the trustee as a fact.[263] It "cannot be presumed from prior or subsequent events, although such events may be some evidence of insolvency".[264]

Under section 4 of Bill C-12, a person is insolvent where:

> (*a*) the property of the person, if it were realized at a fair value, would be insufficient to pay all his certain and liquidated debts whether or not the debts are due; or
>
> (*b*) the person has ceased to pay his certain and liquidated debts generally as they become due.

It should be noted that, in determining whether a debtor is insolvent, his assets are to be estimated not at what they might bring at a sale under legal process, but at a "fair value".[265]

c. *Intent*

(1) *Intent of the Transferee*

In order to set aside a transaction under section 73 of the *Bankruptcy Act*, the trustee must show that the transaction was made "with a view to giving a creditor a preference". The question whether the Act requires only an intent on the part of the insolvent debtor, or an intent on the part of both the debtor and creditor, has been the subject of conflicting legal opinion over the years.[266] It would appear that this question has now been authoritatively settled in the bankruptcy context by the Supreme Court of Canada decision in *Hudson v. Benallack*.[267] In *Hudson*, Dickson J. held that "the view, the only view, with which s. 73(1) of the Act is concerned is that of the insolvent person making the conveyance . . . . Whether or not a conveyance or payment is a fraudulent preference depends entirely on the intention of the debtor".[268] The creditor's cognizance of the debtor's intent was said to be irrelevant. Dickson J. stated that, while "[o]ne can sympathize with the rationale of concurrent intent, which is the desire to protect an innocent creditor who accepts payment of a debt in good faith", it is "hard to reconcile this point of view with the language of the statute, with the history of bankruptcy legislation, and with the right of other innocent creditors to equal protection".[269]

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[262] *Re Selmas - Cromie Ltd.; Gardner v. M/S Apparel Ltd.* (1975), 56 D.L.R. (3d) 578, 21 C.B.R. (N.S.) 10 (B.C.S.C. in Bktcy.) (subsequent references are to 56 D.L.R. (3d)).

[263] *In Re Audio Records Ltd.; Hamel v. Galet* (1962), 4 C.B.R. (N.S.) 99 (Que. S.C. in Bktcy.).

[264] *Re Society Shop Inc.* (1975), 20 C.B.R. (N.S.) 72 (Ont. S.C. in Bktcy.), at 74. See *Re Van Der Liek*, *supra*, note 260, where it was said that the court will not presume insolvency.

[265] In *Rae v. MacDonald*, *supra*, note 29, Rose J. held that a debtor is legally insolvent where he does not have sufficient property subject to execution to pay all his debts if sold under legal process, whereas Cameron J. stated that the debtor's assets were to be estimated not at what they might bring at a forced sale, but at the fair value in cash on the market at an ordinary sale: see *supra*, this ch., sec. 2(b)(ii).

In Bill C-12, sections 172 and 173 deal with a transfer made "with the intent of the debtor to give a preference". In contrast with the case law under the *Bankruptcy Act* and with Bill C-12, a transaction, as indicated earlier, is not void under section 4(2) of the *Assignments and Preferences Act* without proof of concurrent fraudulent intent to obtain an unjust preference.

(2) *Rebutting the Presumptions*

As we have seen, section 73(2) of the *Bankruptcy Act* provides that, where a transaction has the effect of giving a creditor a preference, it shall be presumed *prima facie* to have been made with a view to giving a preference, and the doctrine of pressure is abrogated under such circumstances. There is considerable case law establishing the evidence required to rebut the presumption of intent under section 73(2). In order to rebut the presumption, the debtor must show on a balance of probabilities that his dominant intent was not to give a preference.[270] For example, a number of cases have held that the presumption is rebutted if the dominant intent of the debtor was not to prefer but to carry on business.[271] In these cases, the courts have adopted the attitude that, while a belief that the business could carry on might reflect unwarranted optimism, such optimism is not unknown and negates the existence of a fraudulent intent. However, since each case depends on its own facts,[272] a claim that the dominant intent of the debtor was to keep the company in operation will not always succeed. In *Re Selmas-Cromie Ltd.; Gardner v. M/S Apparel Ltd.*,[273] McKenzie J. quoted with approval the words of Verchere J. in *Re Lock Enterprises Ltd.*[274] to the effect that the intent to continue in business by means of the impugned transfer did not negate the presumption of fraudulent intent, and, if anything, supported it by "giving the bankrupt a motive for paying the creditor in preference to its other creditors and thus offering relevant evidence of the existence of the intent to prefer".

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[266] Cases holding that an intention on the part of both the debtor and creditor is essential include: *Re Bartle* (1941), 22 C.B.R. 260 (Ont. S.C. in Bktcy.); *Re Bell* (1922), 32 Man. R. 9, 67 D.L.R. 66, 2 C.B.R. 271 (C.A.); *Re Webb* (1921), 51 O.L.R. 5, 64 D.L.R. 633, 2 C.B.R. 16 (S.C. in Bktcy.); *Re Demry & Demry, Trustee v. Halland* (1924), 34 Man. R. 534, 4 D.L.R. 1275, 5 C.B.R. 293 (C.A.); *Re Aboud* (1940), 22 C.B.R. 121 (Ont. S.C. in Bktcy.); and *Re Candie Maid Ltd.* (1975), 20 C.B.R. (N.S.) 106 (Ont. S.C. in Bktcy.).

Cases holding that concurrent intent is not necessary include: *Earle Sons & Co. Ltd. v. Crane* (1959), 20 D.L.R. (2d) 468, 44 M.P.R. 71, 38 C.B.R. 115 (Nfld. S.C. in Bktcy.); *Burns v. Royal Bank of Canada* (1922), 51 O.L.R. 564, 69 D.L.R. 608, 2 C.B.R. 241 (S.C. in Bktcy.); and *Re Blenkarn Planer Ltd.* (1958), 14 D.L.R. (2d) 719, 26 W.W.R. 168, 37 C.B.R. 147 (B.C.S.C. in Bktcy.).

[267] *Supra*, note 128.

[268] *Ibid.*, at 182.

[269] *Ibid.*, at 176. The decision in *Hudson v. Benallack* has since been followed in *Re Bear Creek Gravel Ltd.* (1975), 22 C.B.R. (N.S.) 91 (B.C.S.C. in Bktcy.); *Re Amico Bldg. Materials Ltd.* (1976), 22 C.B.R. (N.S.) 111 (Ont. S.C. in Bktcy.); *Re Marathon Music Inc.* (1977), 24 C.B.R. (N.S.) 20, 1 B.L.R. 325 (Ont. S.C. in Bktcy.); and *Re K. & C. Thermoglass Ltd.*, *supra*, note 226.

[270] See *Re McIntyre and Prokop Drugs Limited* (1973), 18 C.B.R. (N.S.) 273 (Sask. Q.B.). Indeed, it would appear that, in determining whether an unjust preference has been given under s. 73(1), the court will require that the making of such a preference be the debtor's dominant intent: see *Re Kovalcik* (1973), 18 C.B.R. (N.S.) 69 (Ont.

The presumption of intent under section 73(2) of the *Bankruptcy Act* may be rebutted where the payment is made in the ordinary course of business, for example, to meet trade bills as they mature. It may also be rebutted where the payment is to discharge a previous obligation or a promise to pay on a particular day.[275]

S.C. in Bktcy.). This requirement to prove the dominant intent of the debtor is a judicial gloss on the legislation, since the Act is silent with respect to this matter.

It would appear that the presumption of fraudulent intent also may be rebutted, for example, in the following cases: where a creditor has obtained a substantial payment because he has been more diligent than other creditors (*Re Houston and Thorton* (1973), 18 C.B.R. (N.S.) 102 (Ont. S.C. in Bktcy.)); and where the insolvent person gives a preference with a view to the improvement of his own financial condition and the condition of his creditors (*Burns v. Royal Bank of Canada*, *supra*, note 266).

[271] See *Re Grimsby Machine Mfg. Co. Ltd.; Anthony v. Associated Steel Specialities Ltd.* (1971), 15 C.B.R. (N.S.) 1 (Ont. C.A.); *Re Hodden Gray Graphics Limited* (1974), 19 C.B.R. (N.S.) 204 (Ont. S.C. in Bktcy.); *Re Shaughnessy Super Market and Codville Co. Ltd.*, *supra*, note 231; *Re Marathon Music Incorporated*, *supra*, note 269; *Re Lee and Ryan Ltd.* (1966), 9 C.B.R. (N.S.) 281 (Nfld. S.C.); *Re D. Elkind Clothing Inc.* (1978), 26 C.B.R. (N.S.) 240 (Ont. S.C. in Bktcy.); and *Re Raymond L. Kaizer Ltd.* (1978), 31 N.S.R. (2d) 665, 28 C.B.R. (N.S.) 250 (S.C., T.D. in Bktcy.).

[272] See *Re Lee and Ryan Ltd.*, *supra*, note 271.

[273] *Supra*, note 262, at 591.

[274] (1971), 16 C.B.R. (N.S.) 83 (B.C.S.C. in Bktcy.), at 86. In *Sigurdson v. Okura & Co., Canada, Ltd.*, [1971] 2 W.W.R. 660 (B.C.S.C. in Bktcy.), Wilson C.J.S.C. dismissed the contention that the dominant motive of the debtor was to do everything possible to keep the company in operation – since the dominant motive of most insolvent traders is to stave off creditors in order to stay in business – and stated (at 670) that he was "concerned not with motive but with intent". The distinction between "motive" and "intent" is hardly self-evident, although his language was approved in *Re Entex International Ltd.* (1975), 21 C.B.R. (N.S.) 157 (B.C.S.C. in Bktcy.). See, also, *In re Siscoe Gold Mines Ltd. v. Lamarre* (1950), 31 C.B.R. 81 (Que. C.A.).

[275] See *Canadian Credit Men's Association Ltd. v. Jenkins* (1927), 62 O.L.R. 281 (App. Div.), and *Re A.W. Brownell and Co.* (1968), 67 D.L.R. (2d) 452, 11 C.B.R. (N.S.) 183 (N.S.S.C. in Bktcy.). See, also, *Re McIntosh-Marshall Equipment Ltd.; Nash v. Western Rock Bit Company Limited* (1968), 12 C.B.R. (N.S.) 60 (Alta. S.C., App. Div.).

Compare these cases to *Re Echlin Press Ltd.* (1968), 11 C.B.R. (N.S.) 258 (Ont. S.C. in Bktcy.), where the sale of operating equipment to the defendant creditor, with whom the debtor had done business for years, was held not to be in the ordinary course of business.

Finally, it is interesting to note that Bill C-12 expressly provides that the presumption of fraudulent intent arising under section 173(2), with respect to non-arm's length transactions executed more than forty-five days and less than one year before the filing of a petition, is rebuttable by proof that the "transfer was made in the normal course of affairs of the debtor in relation to the creditor". Where the transfer occurs less than forty-five days prior to filing, section 173(3)(*b*) requires the preferred creditor to prove, in addition to the above, that the transfer was "in satisfaction of a debt incurred within thirty days of the transfer".

d. Protected Transactions

(1) *Defences under the Bankruptcy Act: Applicability of Section 75*

At first blush, section 75 of the *Bankruptcy Act* appears to have the same object as section 5 of the *Assignments and Preferences Act*, that is, the protection of certain transactions between the debtor and other persons. Section 75 reads:

> 75.-(1) Subject to the foregoing provisions of this Act with respect to the effect of bankruptcy on an execution, attachment or other process against property, and with respect to the avoidance of certain settlements and preferences, nothing in this Act invalidates, in the case of a bankruptcy,
>
> (*a*) any payment by the bankrupt to any of his creditors,
>
> (*b*) any payment or delivery to the bankrupt,
>
> (*c*) any conveyance or transfer by the bankrupt for adequate valuable consideration, or
>
> (*d*) any contract, dealing, or transaction by or with the bankrupt for adequate valuable consideration,
>
> if both the following conditions are complied with, namely:
>
> (*e*) that the payment, delivery, conveyance, assignment, transfer, contract, dealing, or transaction, as the case may be, is in good faith and takes place before the date of the bankruptcy, and
>
> (*f*) that the person, other than the debtor, to, by, or with whom the payment, delivery, conveyance, assignment, transfer, contract, dealing, or transaction was made, executed or entered into, has not at the time of the payment, delivery, conveyance, assignment, transfer, contract, dealing or transaction, notice of any act of bankruptcy committed by the bankrupt.

However, although cases may be found in which preferential transactions contrary to section 73 were upheld under section 75 because the transferee proved "good faith" or "absence of notice",[276] it now appears,

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[276] See *Re Piette et Frère, Inns and Hamel v. La Banque Provinciale du Canada* (1960), 1 C.B.R. (N.S.) 1 (Que. S.C. in Bktcy.), and *Royal Bank v. Lamarre* (1948), 29 C.B.R. 146 (Que. S.C. in Bktcy.), aff'd [1948] Que. K.B. 361, 29 C.B.R. 149 (C.A.).

As noted in Duncan and Honsberger, *Bankruptcy in Canada* (3d ed., 1961), at despite some doubt, that section 75 has no bearing on the applicability of section 73; section 75 cannot be regarded as an exception to section 73 so as to save transactions otherwise void under that section.[277] This view is based on several considerations. First, section 75 is expressly stated to be "[s]ubject to the foregoing provisions of this Act . . . with respect to the avoidance of certain settlements and preferences . . .". That is to say, the protective provisions of section 75 cannot affect, *inter alia*, section 73, dealing with the avoidance of certain preferences. Secondly, the application of section 75 to proceedings taken under section 73 could lead to strange results. Unlike the interpretation given to section 4 of the *Assignments and Preferences Act*, the intent of the debtor alone is relevant under section 73.[278] If the doctrine of concurrent intent is not applicable under that section, then the "good faith" of the creditor of which section 75 speaks cannot logically be a defence in a section 73 action.[279] Thirdly, section 75 refers to transactions between "the bankrupt" and others; there is no mention of an "insolvent person", as is the case in section 73. As noted by Middleton J., in *Briscoe v. Standard Bank of Canada*,[280] the word "bankrupt" is used "in the technical sense and not as the equivalent of an insolvent person". The words "bankrupt" and "insolvent person" are both clearly defined in section 2 of the Act.

The purpose of section 75 has been interpreted by some courts to be the protection of transactions that have taken place between the debtor and other persons between the date of the production of the petition for a receiving order and a judgment awaiting the petition. Owing to the fact that, upon the making of a receiving order, the bankruptcy relates back to the institution of the proceedings, there may be a considerable interval during which a "bankrupt" may carry on business.[281] The title of the trustee relates back to the date of the presentation of the petition. Were it not for section 75, no transaction of the debtor that took place after the presentation of a petition on which a receiving order was made could stand.

485-87 (footnote references omitted), "[i]t is not always possible to separate the cases which turn on the application of [s. 75] from those which rest on the doctrine of concurrent intent. In both lines of cases, questions which are from time to time considered important are: (i) the view or intent of the creditor; (ii) knowledge on the part of the creditor of (*a*) the insolvency of the debtor; (*b*) an act of bankruptcy committed by the debtor; (*c*) circumstances which put him on inquiry".

[277] See *Re Echlin Press Ltd.*, *supra*, note 275; *Re Eastern Land & Housing Ltd.* (1970), 1 N.S.R. (2d) 1005, 14 C.B.R. (N.S.) 55 (S.C. in Bktcy.), aff'd (1971), 3 N.S.R. (2d) 117, 23 D.L.R. (3d) 700 (S.C., App. Div.); *Re Evaporateur Portneuf Inc.*, [1962] Que. Q.B. 218, 3 C.B.R. (N.S.) 182 (Q.B.); *Re Berman and Chapman* (1923), 24 O.W.N. 404, 4 C.B.R. 233 (S.C. in Bktcy.); and *Briscoe v. Standard Bank of Canada* (1923), 24 O.W.N. 174, 53 O.L.R. 623 (App. Div.) (subsequent reference is to 24 O.W.N.).

See, also, Duncan and Honsberger, *supra*, note 276, at 486, and Houlden and Morawetz, *Bankruptcy Law of Canada* (1979), at 4-97 to 4-99.

[278] See *supra*, this ch., sec. 4(b)(ii)c.(1).

[279] *Re Stemac Limited; Goldberg v. Foxboro Co. Ltd.*, [1973] Que. S.C. 56, 18 C.B.R. (N.S.) 243 (S.C. in Bktcy.).

[280] *Supra*, note 277, at 176.

[281] *Re Cohen and Mahlin; Canadian Credit Men's Trust Ass'n Ltd. v. Spivak*, [1927] 1 D.L.R. 577, [1927] 1 W.W.R. 162 (Alta. S.C., App. Div.).

(2) *The Doctrine of Pressure*

As noted earlier, the phrase "fraudulent preference" imports a voluntary act. Therefore, in the absence of statutory provisions abrogating the doctrine of pressure, where there is pressure there can be no fraudulent preference. Under section 73(2) of the *Bankruptcy Act*, which applies to preferences given to related and non-related persons, a *prima facie* presumption of fraudulent intent is raised and the doctrine of pressure is declared to be inapplicable where the effect of a transfer is to give a preference. Section 182 of Bill C-12, which applies to both arm's length and non-arm's length transfers, also abrogates the doctrine in certain circumstances. Section 182 provides that, "[w]here a transfer has the effect of giving a preference to a creditor, evidence that the transfer was made under pressure is not receivable to substantiate such transfer and the debtor may not avail himself of such evidence to support such transfer".

(3) *Substitution of Property*

It will be recalled that section 5(5)(*c*) of the Ontario *Assignments and Preferences Act* provides that nothing in that Act "applies to the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors . . .".[282] An analogous, but broader, provision appears in Bill C-12. Section 177 of Bill C-12 provides as follows:

> 177.-(1) Where a person has released or returned to a debtor property previously transferred by the debtor in a transfer that is not a preference and the debtor substitutes other property for the property released or returned, the substitution is a transfer that is not a preference except to the extent that the value of the substituted property as of the date at which the person agrees to accept the substituted property for the property released or returned exceeds the value of the property released or returned.
>
> (2) For the purposes of subsection (1), the release or return and substitution of property need not take place simultaneously where the release or return is made in contemplation of the substitution and the substitution is made within a reasonable time after the release or return.

It bears noting that, in both section 5(5)(*c*) and section 177, the transaction would be saved only where the two items of property in question have at least the same value, so that the effect of the transaction would not have been to prejudice the creditors.

(4) *Debtor's Solvency Subsequent to a Transaction*

Another saving provision in Bill C-12 deals with the situation where, subsequent to the impugned transaction but before the date of bankruptcy, the debtor becomes solvent. Under section 179, this intervening solvency will serve to protect the transaction. Section 179 provides as follows:

> 179. A transfer, payment of dividend or redemption or purchase of shares

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[282] See *supra*, this ch., sec. 3(d)(iv)d.(2).

> may not be set aside or be subject to review pursuant to sections 168 to 178 where it is proved that, at any time after the transfer, payment of dividend or redemption or purchase of shares was made and before the date of bankruptcy, the person who subsequently became a bankrupt was solvent.

While this provision is presumably premised on the principle that the intervening solvency would permit creditors to satisfy their debts without recourse to the transferred property, and that the failure to do so should justifiably bar creditors from impeaching the transfer should the debtor subsequently become insolvent, it bears emphasizing that not all creditors are judgment creditors or otherwise in a position to seek payment of their debts during the period of insolvency.

e. Transactions between Related Persons

With respect to preferences, the *Bankruptcy Act* distinguishes between preferential transactions in favour of persons related to an insolvent debtor and those in favour of non-related persons.[283] Section 4 defines in considerable detail which persons are related to each other.

As we have seen, sections 172 and 173 of Bill C-12 differentiate between preferential transactions at arm's length and those otherwise than at arm's length. The definition of these terms is found in sections 7 and 8 of the Bill, which, in view of the recommendations made later in this chapter, are here reproduced in full:[284]

> 7.-(1) For the purposes of this Act,
>
> (*a*) it is a question of fact whether persons not related to each other were, at a particular time, dealing with each other at arm's length; and

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[283] Prior to the enactment of s. 74 (see S.C. 1966-67, c. 32, s. 11), which deals with preferences to related persons, only fraudulent preferences that had occurred within three months of bankruptcy could be attacked (see s. 73). There had been considerable dissatisfaction with the three month limitation, since in many cases bankruptcies were delayed until the three months had elapsed to prevent the avoidance of preferential transactions. This was especially true where a preference had been given to a person or a corporation having a close relationship with the debtor.

The enactment of s. 74 has only partially remedied the problem. If the trustee wishes to attack a transaction that occurred more than three months prior to, but within one year of, bankruptcy, he must prove that the creditor involved was related. If the transaction sought to be set aside took place more than three months before bankruptcy and not with a related person, resort must be had to the remedies provided by provincial preference statutes.

[284] Although the *Assignments and Preferences Act* contains no express provision with respect to transactions between related persons, some cases have held that the court should exercise more than the usual care in examining whether a transaction between related persons is void. In *Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd.*, *supra*, note 255, the Alberta Supreme Court, Trial Division, considered the validity of a transaction between two corporations controlled by the same two persons who were the sole shareholders, directors and officers of both companies.

See, also, *supra*, this ch., sec. 2(b)(iii)a, concerning transactions between near relatives.

(*b*) persons related to each other are deemed not to deal with each other at arm's length.

(2) For the purposes of this Act, individuals are related to each other

(*a*) where one is married to the other; or

(*b*) where one is connected with the other by blood relationship, marriage or adoption,

(i) in direct line, or

(ii) in collateral line to the degree existing between brothers and sisters, whether they have the same parents or only the same father or mother.

(3) For the purposes of this Act,

(*a*) 'adoption' includes *de facto* adoption;

(*b*) 'blood relationship' includes an illegitimate relationship;

(*c*) two individuals of the opposite sex are deemed to be married to one another where they live together as husband and wife; and

(*d*) an individual is deemed to have the same relationship by marriage to the relatives of his spouse during the existence of the marriage and thereafter as his spouse has by blood relationship.

8.-(1) For the purposes of this section,

(*a*) a person or group of persons controls a corporation where the person or group

(i) holds more than fifty per cent of the issued shares of the corporation having full voting rights under all circumstances, or

(ii) holds fifty per cent of the issued shares of the corporation having full voting rights under all circumstances and the person or a member of the group is entitled to cast a deciding vote at a meeting of shareholders;

(*b*) 'related group' means a group of persons each member of which is related to every other member of the group;

(*c*) 'unrelated group' means a group of persons that is not a related group; and

(*d*) a person who has a contractual right, either immediately or in the future and either absolutely or contingently to, or to acquire, shares of a corporation or to control the voting rights attached to shares of a corporation, shall be deemed to have the same position in relation to the control of the corporation as if he owned the shares.

(2) Paragraph (1)(*d*) does not apply where the right of the person to, or to acquire, shares of a corporation or to control the voting rights attached to shares of a corporation is not exercisable until the death of an individual designated in the contract.

(3) Paragraph (1)(*d*) does not apply where

(*a*) the corporation is a party to a contract with another person and the contract provides that on the fulfilment of a condition or the happening of an event that it is reasonable to expect will be fulfilled or will happen,

(i) the other person ceases to have an interest in shares of the corporation, and

(ii) the shares are acquired by a person with whom the other person deals at arm's length; and

(*b*) the chief purpose for which a person has an interest in shares of the corporation is as a result of a security interest in respect of

(i) a loan made by the person, the whole or any part of which is outstanding, or

(ii) any shares issued by the corporation that are held by the person and that are, under the contract, required to be redeemed by the corporation or purchased by another person with whom the vendor of the shares deals at arm's length.

(4) Where a corporation is controlled by a person, it is related to

(*a*) the person who controls it; and

(*b*) any person related to the person who controls it.

(5) Where a corporation is controlled by a related group, it is related to

(*a*) each member of the group; and

(*b*) any person related to a member of the group.

(6) Where a corporation is controlled by an unrelated group, it is related to any person

(*a*) who, being a member of the group, is related to each other member; or

(*b*) who, not being a member of the group, is related to each member of the group.

(7) Without restricting the generality of subsections (4) to (6), two corporations are related to each other

(*a*) where they are related to the same person or controlled by the same person or group; or (*b*) where one corporation is controlled by an unrelated group and the other corporation is controlled by another unrelated group and each member of one group is a member of or related to at least one member of the other group.

f. Tracing the Property and Proceeds

Both the *Bankruptcy Act* and Bill C-12 protect transferees subsequent to the original, impugned transaction, where they have paid "in good faith adequate valuable consideration". Subsections (1) and (2) of section 76 of the *Bankruptcy Act* provide for the recovery, from an original or a subsequent transferee, of the property, its value, or the proceeds of a sale of the property. Section 76(3) then provides as follows:

> 76.-(3) Notwithstanding subsection (1), where any person to whom the property has been sold or disposed of has paid or given therefor in good faith adequate valuable consideration he is not subject to the operation of this section but the trustee's recourse shall be solely against the person entering into the transaction with the bankrupt for recovery of the consideration so paid or given or the value thereof.

Under Bill C-12, section 175(1) gives certain powers to the court where it sets aside a transfer. For example, section 175(1)(*a*) provides that the court may make an order "empowering the trustee to recover the property or the value thereof" not only from the original transferee, but also, "subject to subsection (2), from any other person to whom the property has been transferred". Section 175(2) reads as follows:

> 175.-(2) Subsection (1) does not apply where any person to whom property has been transferred paid or gave in good faith adequate valuable consideration for the property and any recourse of the trustee is solely against the person party to the transfer with the bankrupt.

(iii) Fraudulent Conveyances

a. General Scheme of Existing and Proposed Legislation

Aside from utilizing the provisions of the *Fraudulent Conveyances Act* and section 4(1) of the *Assignments and Preferences Act*, a trustee in bankruptcy may seek to impeach a "settlement" under section 69 of the *Bankruptcy Act*, subsections (1) and (2) of which provide as follows:

> 69.-(1) Any settlement of property, if the settlor becomes bankrupt within one year after the date of the settlement, is void against the trustee.
>
> (2) Any settlement of property, if the settlor becomes bankrupt within five years after the date of the settlement, is void against the trustee if the trustee can prove that the settlor was, at the time of making the settlement, unable to pay all his debts without the aid of the property comprised in the settlement[285] or that the interest of the settlor in the property did not pass on the execution thereof.

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[285] In other words, the settlement itself has rendered the debtor insolvent, whereas before

While there is no statutory definition of "settlement", and while many bankruptcy courts have expressed the view that the meaning of the term is unclear, to the point that there seems to be no generally accepted definition,[286] it has been described as referring to a transfer involving a trust.[287] But other formulations abound. For example, in *Re Bozanich, A.H. Boulton Co. Ltd. v. Trusts & Guarantee Co. Ltd.*,[288] the Court, having regard to the English bankruptcy provisions – which were the ancestors of the relevant Canadian sections – narrowly circumscribed the meaning of "settlement" notwithstanding that it was defined in the relevant Canadian legislation to "include any conveyance or transfer of property".[289] Duff C.J. noted that the "well settled" interpretation of the term was that it implied an intention that the property should be retained or preserved for the benefit of the donee in such a form that it could be traced.[290] Accordingly, it would not include all conveyances or transfers. Rinfret J. stated that he "would incline to the opinion that, generally speaking, 'settlement' involves the idea of a clear gift, or that type of cases where provision is made for a trust of some sort".[291]

In addition to voiding a settlement under section 69, section 78(1) of the present Act provides that the court, upon the application of a trustee, may inquire into the adequacy of the consideration received in any "reviewable transaction" entered into within twelve months preceding the bankruptcy. Section 3(1) provides that the term "reviewable transaction" means a non-arm's length transaction. Under section 78(2), if the consideration was "conspicuously" inadequate, the trustee could be awarded judgment for the difference between the consideration actually received and the fair market value of the property.

Finally, reference should be made to the protection of transferees of property who purchased the property subsequent to the original transaction. As we have seen,[292] section 76(3) of the *Bankruptcy Act* precludes the recovery of the property, its value, or the proceeds of its sale from a subsequent transferee who paid "in good faith adequate valuable consideration".

The relevant provisions of Bill C-12 are wider than those of the pres-

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the settlement he had sufficient assets to pay *all* his debts in full. Compare s. 69(2) to the broader language of s. 168(*c*) of Bill C-12, where reference is made to a gift by a debtor who is either "insolvent or unable to pay his debts without the aid of the property comprised in the gift".

[286] See, for example, *Re Vansittart, Ex parte Brown*, [1893] 1 Q.B. 181, at 182-84, [1891-94] All E.R. Rep. 1111, and *Re Tankard, Ex parte Official Receiver*, [1899] 2 Q.B. 57, at 59-61, 68 L.J.Q.B. 670.

[287] See *Re Cohen and Lyons; Can. Credit Men's Trust Ass'n Ltd. v. Spivak*, [1926] 3 D.L.R. 942, [1926] 3 W.W.R. 34 (Alta. S.C. in Bktcy.), rev'd *supra*, note 281.

[288] *Re Bozanich, A.H. Boulton Co. Ltd. v. Trusts & Guarantee Co. Ltd.*, [1942] S.C.R. 130, [1942] 2 D.L.R. 145 (subsequent references are to [1942] S.C.R.).

[289] *Bankruptcy Act*, R.S.C. 1927, c. 11, s. 62(3).

[290] *Supra*, note 288, at 135. See, also, *Re Beaulieu*; *Perras v. Pilon* (1942), 24 C.B.R. 197 (Que. C.A.).

[291] *Supra*, note 288, at 140.

[292] See *supra*, this ch., sec. 4(b)(ii)f.

ent Act. Sections 168 and 169 of Bill C-12, respectively, give the court power to set aside certain "gifts" and to review certain "transfers".[293] Different rules apply to different situations, having regard, for example, to when the gift was made, the financial status of the debtor, whether the parties were acting at arm's length, and whether the transfer was made in the normal course of affairs.

In reviewing or setting aside a transfer, the court has several options, contained in section 169(4) and (5) and section 175(1) of Bill C-12. With respect to the powers of the court in reviewing a transaction, section 169(4) and (5) of Bill C-12 provides as follows:

> 169.-(4) Where, in reviewing a transfer pursuant to this section, the court finds that one consideration was conspicuously greater in fair value than the other to the detriment of the party who subsequently became a bankrupt, the court may
>
> (*a*) determine the amount of the difference in the fair values and give judgment for an amount not exceeding the amount of the difference to the trustee against the other party;
>
> (*b*) determine the amount of the difference in the fair values and reduce the claim of the other party against the estate by an amount not exceeding the amount of the difference; or
>
> (*c*) make an order declaring the transfer to be void and restoring each party to the transfer in so far as possible to the state that he was in immediately prior to the transfer.[294]
>
> (5) Where, in reviewing a transfer pursuant to this section, the court finds that the effect of the transfer was to impede, obstruct, delay or defraud the creditors or any of them, the court may set aside the transfer and restore each party to the transfer in so far as possible to the state that he was in immediately prior to the transfer.

It would appear that the court would not be empowered under these provisions to set aside or declare void a transfer without at the same time restoring each party "in so far as possible to the state that he was in immediately prior to the transfer".[295] Whether or not the draftsman intended such an automatic linkage, the power to restore the parties to the *status quo ante* essentially obviates the problem under provincial legislation, where, generally speaking, a transferee who has paid valuable consideration apparently cannot have this consideration returned to him when the transaction is avoided.[296]

Section 175(1) of Bill C-12, reproduced above,[297] deals with the powers of the court where it "sets aside" a transfer. However, it bears repeating that, like section 76(3) of the *Bankruptcy Act*, section 175(2), discussed earlier,[298] prevents the tracing of the property or its value in the hands of a subsequent transferee who has paid "in good faith adequate valuable consideration".

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[293] The terms "gift" and "transfer" are both defined in s. 2(1).

[294] Concerning the valuation of the consideration given by the debtor and the transferee for the purposes of s.s.(4), see s. 169(3).

[295] See ss. 169(4)(*c*) and 169(5).

[296] But see ss. 5(4) and 5(5)(*b*) of the Ontario *Assignments and Preferences Act*, discussed *supra*, this ch., sec. 3(d)(iv)d.(1).

[297] See *supra*, at 179.

b. Intent

Under the *Bankruptcy Act*, neither the "settlement" provisions in section 69 nor the "reviewable transaction" provisions in section 78 require the trustee to prove the debtor's fraudulent intent.[299] The same is true under the "gift" provisions, the non-arm's length transfer provisions, and certain arm's length transfer provisions of Bill C-12.[300] This is in contrast to the provisions relating to certain other arm's length transfers under section 169(1)(*b*) of Bill C-12[301] and to the *Fraudulent Conveyances Act*. The phrase "with the intent known to both parties" in section 169(1)(*b*) makes it clear that the intent of both the debtor and the transferee must be shown.

c. Transactions between Related Persons

As in the case of the preference provisions, the *Bankruptcy Act* provisions relating to fraudulent conveyances employ the concept of "related persons". Section 78 deals with a "reviewable transaction", which, by section 3(1), is deemed to be a non-arm's length transaction. Section 3(3) then provides that "[p]ersons related to each other within the meaning of section 4[302] shall be deemed not to deal with each other at arm's length while so related". Similarly, section 169 of Bill C-12 speaks in terms of arm's length and non-arm's length transfers, which, again, are partly defined in terms of relationship.[303]

d. Protected Transactions

Section 69(3) of the *Bankruptcy Act* removes from the ambit of section

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[298] See *supra*, this ch., sec. 4(b)(ii)f.

[299] It will be recalled, however, that the debtor's "good faith" is relevant under the narrow protective provisions of s. 75.

[300] See, respectively, ss. 168, 169(2), and 169(1)(*a*) of Bill C-12.

[301] Section 169(1)(*b*) provides:

> 169.-(1) Where persons who are at arm's length enter into a transfer and one of the persons subsequently becomes a bankrupt, the court, on application of the trustee, may review the transfer where it was entered into
>
> . . . .
>
> (*b*) less than six years before the date of filing the petition and with the intent known to both parties, to impede, obstruct, delay or defraud a creditor.

[302] Section 4 defines what is meant by a "related group", "unrelated group", and "related persons".

[303] The relevant provisions of Bill C-12 – that is, ss. 7 and 8 – are reproduced *supra*, at 186-89.

69 any settlement made "before and in consideration of marriage", or "in favour of a purchaser or encumbrancer in good faith and for valuable consideration", or "on or for the wife or children of the settlor of property that has accrued to the settlor after marriage in right of his wife or of his children". Under section 169(1)(*a*) of Bill C-12, a court may not review certain arm's length transfers entered into "in the normal course of affairs". In addition, as indicated earlier,[304] section 179 adds a new saving provision in respect of certain transactions where, after the transaction and before the date of bankruptcy, the debtor becomes solvent.

(iv) Conclusion

Leaving aside the statutory protective provisions, a significant difference between the present *Bankruptcy Act* and Bill C-12, on the one hand, and the *Fraudulent Conveyances Act* and *Assignments and Preferences Act*, on the other hand, lies in the greater extent to which the existing and proposed bankruptcy legislation makes use of deeming provisions to invalidate certain transactions, irrespective of the debtor's intent. By way of contrast, both provincial statutes expressly require proof of a fraudulent intent on the part of the debtor and, in some cases, on the part of the transferee as well. Under the *Fraudulent Conveyances Act*, there is a presumption of fraudulent intent where an insolvent debtor makes a gift, or, put more broadly, where the effect of the conveyance was to defeat creditors; however, the presumption is rebuttable. Under section 4(3) of the *Assignments and Preferences Act*, there is a presumption of fraudulent intent where impeachment of the preference occurs within sixty days of its execution; again, however, the presumption is rebuttable.

A second notable difference, at least between Bill C-12 and the two provincial statutes, is the greater flexibility in respect of the powers of the court under the Bill. The jurisdiction to restore the *status quo ante* is but one feature of the panoply of powers accorded to a court under the proposed bankruptcy statute. Other powers – for example, under section 169(4)(*a*) of Bill C-12 – permit the court to do justice in individual situations. As a general proposition, it may be said that both the present and proposed bankruptcy legislation provide more detail in respect of the rights against the original transferee and those claiming by, from, or under him. Other than section 12 of the *Assignments and Preferences Act*, applicable also to proceedings under the *Fraudulent Conveyances Act*, the provincial statutes are silent in respect of many such relevant matters.

The greater ease with which certain transactions are set aside under the bankruptcy provisions may well reflect the very nature of bankruptcy itself. Bankruptcy represents, or is intended to represent, a new plateau for debtors, where there will be at least an attempted resolution of their troubled financial affairs and an opportunity to begin afresh. A clearing of the financial slate, often by payment of a very small fraction of the existing debts, may require a stricter and more thoroughgoing investigation into past transactions, particularly where the transactions are with relatives of the debtor or are otherwise not at arm's length. Prior to bankruptcy, however, there is, at least in theory, no comparable discernible break. Debts not satisfied after one seizure or garnishment are not discharged; they continue to be an obligation that the debtor ultimately must fulfil unless bankruptcy intervenes or the parties enter into some informal arrangement. Perhaps, under these circumstances, where the debtor may be continuing in business or continuing his other financial activities, there is thought to be somewhat less need for a strict regime respecting fraudulent transactions.

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[304] See *supra*, this ch., sec. 4(b)(ii)d.(4).

In some instances, of course, the distinction seems more apparent than real. Debts not collected by traditional enforcement measures may have to be written off as bad debts. Accordingly, the inability to attack a transaction successfully may be as significant outside of bankruptcy as it is within bankruptcy. Moreover, a more lenient enforcement regime *vis-à-vis* the bankruptcy legislation may simply force creditors to pursue bankruptcy – in a sense, one might say prematurely – as the only means of realizing the debts due to them. The relationship between traditional, pre-bankruptcy enforcement and bankruptcy is a close one and must be borne in mind when making proposals for reform of provincial legislation.

(c) THE AMERICAN UNIFORM FRAUDULENT CONVEYANCE ACT

In addition to legislation across Canada and in England, the Commission has examined the United States Uniform Fraudulent Conveyance Act,[305] which has been adopted by twenty-five states, including California, Michigan, New York, Pennsylvania, and Wisconsin. Like most legislation dealing with conveyances in fraud of creditors, it is based, in part, on 13 Eliz., c. 5.

In the United States, insofar as preferences are concerned, and aside from certain provisions in the Uniform Act dealing with conveyances to satisfy or secure antecedent debts, there is a substantial lack of uniformity from state to state regarding the treatment accorded to a debtor's preference of one creditor over other creditors. Generally speaking, where there is no statutory prohibition, the common law rule applies. This rule, affirmed by statute in some jurisdictions,[306] provides that, in the absence of fraud, an insolvent or financially embarrassed debtor may prefer one or more of his creditors.

Whereas American jurisdictions often vary greatly in their treatment of preferences, there is much greater consistency in regard to fraudulent conveyances. The adoption of the Uniform Fraudulent Conveyance Act in many states has been largely responsible for this situation.

The American Uniform Law Commissioners were of the opinion that the presumptions of law concerning intent were used to an extreme and, ultimately, were a substitute for sound judicial reasoning. The Uniform Act codifies only certain presumptions and seeks to preclude others. The Commissioners' Prefatory Note to the Uniform Act expresses the necessity for, and the nature of, the reforms manifested in the Act, and deserves to be quoted:[307]

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[305] *Supra*, note 9.

[306] See, for example, §3432 of the California Civil Code, which provides:

> 3432. A debtor may pay one creditor in preference to another, or may give to one creditor security for the payment of his demand in preference to another.

> The confusions and uncertainties of the existing law which have been referred to are due primarily to three things:
>
> > First, the absence of any well recognized, definite conception of insolvency.
> >
> > Second, failure to make clear the persons legally injured by a given fraudulent conveyance.
> >
> > Third, the attempt to make the Statute of Elizabeth cover all conveyances which wrong creditors, even though the actual intent to defraud does not exist.
>
> The Statute of Elizabeth condemns conveyances as fraudulent only when made with the 'intent' to 'hinder, delay or defraud.' There are many conveyances which wrong creditors where an intent to defraud on the part of the debtor does not in fact exist. In order to avoid these conveyances, the courts have called to their assistance presumptions of law as to intent, and in equity have pushed presumption of fraud as a fact to an unwarranted extent; with the result that while in the main decisions under the facts do justice, the reasoning supporting them leaves much to be desired.
>
> In the Act as drafted all possibility of a presumption of law as to intent is avoided. Certain conveyances which the courts have in practice condemned, such as a gift by an insolvent, are declared fraudulent irrespective of intent. On the other hand, while all conveyances with intent to defraud creditors (see Section 7) are declared fraudulent, it is expressly stated that the intent must be 'actual intent, as distinguished from intent presumed as a matter of law.'
>
> In most states the bill if enacted will not so much change the law as clearly define what heretofore has been indefinite. There is, indeed, on a few questions, a sharp conflict between the law of different jurisdictions; especially there are a few states, such as Alabama and Kentucky, which adhere to an early rule of great severity, making any gift voidable as to existing creditors if thereafter the donor becomes insolvent; though at the time of the gift he had ample means remaining to meet all his obligations. The Act adopts the view of the great majority of jurisdictions that such a gift is not fraudulent.
>
> In the main, however, the great benefit from the enactment of the Statute will be to remove some confusion of legal thought, which now renders the law on many points uncertain in all jurisdictions, and substitute for these uncertain rules both certain and uniform ones.

The provision in the Uniform Fraudulent Conveyance Act closest to section 2 of the Ontario *Fraudulent Conveyances Act* is section 7:

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[307] Uniform Laws Annotated, Vol.7A (1978), at 162-63.

> 7. Every conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors.[308]

Leaving aside the requirement of "actual intent" and, therefore, the apparent abolition of certain presumptions, it should be noted that cases under this section have avoided transactions even where the debtor was solvent and had received fair and adequate consideration. In some cases, it has been said that the effect of the transaction is irrelevant; only the "actual intent" of the debtor must be proved. In other words, a conveyance that does not in fact prejudice creditors may be impeached successfully.

At the other extreme is section 4 of the Act, which provides as follows:

> 4. Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent[309] is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration.

The importance of section 4 will be recognized immediately. Where a debtor is insolvent at the date of the conveyance, or is rendered insolvent thereby, and the conveyance is made without "fair consideration", the conveyance is deemed to be fraudulent. Since such a conveyance will invariably have the effect of defeating creditors, section 4 adopts a regime premised on the effect of the conveyance, rather than the intent of the debtor. Accordingly, section 4 is rather reminiscent of the orthodox *Freeman v. Pope* doctrine,[310] generally eschewed of late by a majority of courts.

Relevant to section 4 is section 3, the provision respecting "fair consideration". Section 3 provides as follows:

> 3. Fair consideration is given for property, or obligation,
>
> (a) When in exchange of such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed or an antecedent debt is satisfied, or
>
> (b) When such property, or obligation is received in good faith to secure a present advance or antecedent debt in amount not disproportionately small as compared with the value of the property, or obligation obtained.

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[308] The term "creditor" is defined in §1 to mean "a person having any claim, whether matured or unmatured, liquidated or unliquidated, absolute, fixed or contingent".

[309] Section 2(1) provides that "[a] person is insolvent when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured". Concerning insolvency under provincial law and under bankruptcy legislation, see, respectively, *supra*, this ch., secs. 2(b)(ii) and 4(b)(ii)b.

[310] *Supra*, this ch., sec. 2(b)(iii)b.

For our purposes, reference should be made to the use of the phrase "in good faith". Section 4 unambiguously states that a transaction may be fraudulent "without regard to [the debtor's] actual intent". Accordingly, while in section 3(a) the phrase "in good faith" conceivably could apply, as a matter of grammatical construction, to either the debtor or the transferee, it would seem more reasonable to assume that it applies to the latter. This conclusion may be buttressed somewhat by section 3(b), where it appears clearer that the phrase applies to the transferee.[311] Consequently, not all transferees for fair value are protected. Why the section introduces the transferee's good faith is not clear, at least in the fraudulent conveyance context, where the concept serves to dilute the force of the legislation making the debtor's intent irrelevant. With respect to an allegedly fraudulent conveyance, if a "fair equivalent" has been given, how have creditors suffered? Conversely, where the consideration is not a "fair equivalent", what difference should it make that the transferee was or was not "in good faith"? The absence of a "fair equivalent" would doom the conveyance by an insolvent debtor; the transferee's good faith would not appear to be relevant as a practical matter in any event.

Reference also should be made to several further provisions in the Uniform Fraudulent Conveyance Act. For example, section 5 deals with the effect of a conveyance made by a person in business. It, too, disregards the debtor's intent and focuses on the effect or likely effect of the impugned transaction:

> 5. Every conveyance made without fair consideration when the person making it is engaged or is about to engage in a business or transaction for which the property remaining in his hands after the conveyance is an unreasonably small capital, is fraudulent as to creditors and as to other persons who become creditors during the continuance of such business or transaction without regard to his actual intent.

Section 6 further spells out the effect of a conveyance by someone who intends to incur debts:

> 6. Every conveyance made and every obligation incurred without fair consideration when the person making the conveyance or entering into the obligation intends or believes that he will incur debts beyond his ability to pay as they mature, is fraudulent as to both present and future creditors.

These two provisions resemble Ontario case law permitting a subsequent creditor to attack a conveyance where the debtor has entered into a "risky" or "hazardous" enterprise that was likely to attract a considerable number of creditors, or where the debtor intended to defeat future creditors.

One final interesting feature of the Uniform Fraudulent Conveyance Act concerns creditors' remedies. Sections 9 and 10 deal, respectively, with the rights of creditors with claims that have "matured" and with claims that have "not matured". A matured claim, while not defined in the Uniform Act, has been defined elsewhere to mean a "[c]laim which is unconditionally due and owing".[312] A matured claim need not necessarily have been reduced to judgment, although a judgment debt is clearly a matured claim. Sections 9 and 10 provide as follows:

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[311] With respect to the good faith or knowledge of the transferee, see, also, §9(1) of the Act, discussed *infra*, this sec.

> 9.-(1) Where a conveyance or obligation is fraudulent as to a creditor, such creditor, when his claim has matured, may, as against any person except a purchaser for fair consideration without knowledge of the fraud at the time of the purchase, or one who has derived title immediately or mediately from such a purchaser,
>
> (a) Have the conveyance set aside or obligation annulled to the extent necessary to satisfy his claim, or
>
> (b) Disregard the conveyance and attach or levy execution upon the property conveyed.
>
> (2) A purchaser who without actual fraudulent intent has given less than a fair consideration for the conveyance or obligation, may retain the property or obligation as security for repayment.
>
> 10. Where a conveyance made or obligation incurred is fraudulent as to a creditor whose claim has not matured he may proceed in a court of competent jurisdiction against any person against whom he could have proceeded had his claim matured, and the court may,
>
> (a) Restrain the defendant from disposing of his property,
>
> (b) Appoint a receiver to take charge of the property,
>
> (c) Set aside the conveyance or annul the obligation, or
>
> (d) Make any order which the circumstances of the case may require.

Section 9(1)(b) permits a creditor to "[d]isregard the [fraudulent] conveyance and attach or levy execution upon the property conveyed". Presumably, this clause would apply not only to the original transfer from the debtor, but also to a subsequent transfer from the original transferee, exempting only "a purchaser for fair consideration without knowledge of the fraud at the time of the purchase, or one who has derived title immediately or mediately from such a purchaser". Accordingly, it appears that even a purchaser with knowledge of the fraud may retain the property so long as he purchases it from a *bona fide* purchaser to whom the protective provisions of section 9 apply.

A further interesting feature of section 9 is contained in subsection (2), which permits a "purchaser . . . without fraudulent intent [who] has given less than a fair consideration" to "retain the property or obligation as security for repayment". Section 9(2) is analogous to sections 5(4) and

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[312] *Black's Law Dictionary* (5th ed., 1979).

5(5)(*b*) of the *Assignments and Preferences Act*, although, significantly, section 9(2) is not restricted to secured parties. The Ontario provisions permit a secured creditor who has given up his security in consideration of a payment by the debtor to have the security restored or its value made good to him before he is obliged to return the payment. Sections 5(4) and 5(5)(*b*) attempt to place the secured party in the same position that he was in prior to the impeached transaction; however, other transferees are denied express statutory protection.[313]

5. PROPOSALS FOR REFORM IN NEW BRUNSWICK

In 1976, the Law Reform Division of the New Brunswick Department of Justice published its *Third Report of the Consumer Protection Project*, Volume II, *Legal Remedies of the Unsecured Creditor After Judgment*. A substantial portion of the Report dealt with voidable transactions under 13 Eliz., c. 5 (in force in New Brunswick) and the *Assignments and Preferences Act*.[314] Recommendations for reform appeared in two sections of the Report, one dealing with reform based on the retention of a similar type of enforcement regime to the existing New Brunswick regime, the other based on the adoption of a totally new type of enforcement regime.[315] In the following two sections, we shall deal with the main recommendations concerning voidable transactions proposed in the New Brunswick Report.

(a) RECOMMENDATIONS FOR REFORM UNDER THE EXISTING ENFORCEMENT SYSTEM

From a perusal of the New Brunswick proposals, it seems clear that fundamental reform was not believed to be essential in the area of voidable transactions. An attempt was made to codify, amend, clarify and, in some instances, expand the existing statute and case law. The merits of a statutory regime based on the debtor's fraudulent intent, aided by a plethora of presumptions and inferences, were nowhere questioned. Nor was there any detailed consideration given to alternative statutory models.

The generally traditional focus of the proposals was made clear in the first two recommendations:[316]

> It is recommended that the existing provisions of the *Assignments and Preferences Act* making void transactions by insolvent persons with intent to defeat creditors[317] be replaced by new legislation making transactions to defeat

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[313] With respect to ss. 5(4) and 5(5)(*b*), see *supra*, this ch., sec. 3(d)(iv)d.(1). With respect to the rights of transferees generally, see *ibid.*, sec. 2(b)(vii)b.

[314] R.S.N.B. 1973, c. A-16. See *supra*, this ch., sec. 4(a)(iii).

[315] For a brief description of these regimes, see Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters* (1981) (hereinafter referred to as "Commission Report"), Part I, at 107-09.

[316] New Brunswick Report, *supra*, note 30, at 154. A summary of recommendations concerning voidable transactions begins at page 154 of the New Brunswick Report. Where the recommendations have been reproduced in this chapter, the original emphasis has been deleted.

[317] The term "creditor" was to be "generally defined to include a person who has a cause of action against another person, without regard to whether the claim is liquidated or whether a judgment has been obtained upon the cause of action; and . . . the term

creditors voidable on the basis of intent to defeat creditors,[318] without regard to the solvency of the debtor.

It is recommended that the new legislation codify the main principles of the judicial interpretation of the existing legislation with revisions as proposed in

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'creditor' [was to] be defined for the purpose only of the new legislation regarding transactions to defeat creditors to include existing and future creditors": *ibid.*, at 154. This definition would conform to the provisions, as interpreted, of the *Fraudulent Conveyances Act*, which refers to "creditors or others", rather than to the provisions of the *Assignments and Preferences Act*, under which only existing judgment creditors or creditors with liquidated claims may impeach a transaction. In respect of "future", or subsequent, creditors, the Report said (at 141, *n*. 203):

> If subsequent creditors are entitled to the benefits of the English statute, it is uncertain why the payment of existing creditors can deprive them of those benefits. The answer probably lies, not in the area of what creditors are entitled to benefit, but in the principle that a debtor purges his improper intent by paying his existing creditors. . . .
>
> Any anomaly that exists in this type of situation should be removed by the recommendations for covering subsequent creditors generally.

The Report then continued (at 143-44, *n*. 206):

> It seems unjust that a scheme to avoid a subsequent creditor should succeed because there is no creditor outstanding whose claim existed at the date of the impugned transaction. The subsequent creditor might have a tort action for deceit or fraud, apart from the legislation, but such a claim would be difficult to establish. If the intent to defeat creditors is related to a creditor's claim or claims of a type into which the creditor's claim falls, the creditor should be able to attack the transaction, whether or not his or any other claim was outstanding at the time of the transaction.
>
> . . . .
>
> One possible method of protecting the subsequent creditor who is entitled to protection is to enable all subsequent creditors to attack the voidable transaction. This in turn raises other problems of general policy. Once the transaction as [*sic*] been made, it is arguable that subsequent creditors have no just claim since they extended credit on the basis of the debtor's position after the transaction.
>
> On the other hand, under the present law, if an existing creditor has a transaction set aside, a subsequent creditor would be able to share in the proceeds under the *Creditors Relief Act*. Present law generally does not discriminate between unsecured creditors on the basis of when their claim arises. The only notable exception is under the *Bankruptcy Act* where only claims originating from transactions prior to bankruptcy are entitled to share in the estate.

[318] Even in the context of a regime founded on fraudulent intent, the New Brunswick Report made a recommendation that comprehends an element of a regime founded on the effect of a transaction. The Report recommended (*ibid.*, at 156) that "provision be made that the intent to defeat creditors is purged only by the payment of all outstanding creditors, whether their claims arose prior to or subsequent to the voidable transaction, and the payment of all creditors contemplated at the time of the voidable transaction".

The rationale for this recommendation – which the Report said (*ibid.*, at 121-22, *n*. 158) would essentially codify existing law – was stated to be as follows (at 121, *n*. 158):

> If [the concept of purging is not retained], a transaction made with improper intent might be challenged at any time up until the [proposed] limitation period [six years from the date of the transaction] has run. It would not matter how much the debtor had repented his original intent and faithfully paid his creditors in the meantime, or how unrelated his debts when he does ultimately default are to those existing when he made the voidable transaction.

subsequent recommendations, and that, to avoid confusion between the new legislation and the English Statute of Elizabeth, provision be made that the English Statute of 13 Elizabeth, chapter 5, is no longer in force in New Brunswick.

Leaving aside the reaffirmation of the pivotal doctrine of fraudulent intent in the first recommendation, the abolition of insolvency as a jurisdictional fact would not involve as major a departure from the present law as would seem at first. The insolvency of the debtor is not mentioned in the *Fraudulent Conveyances Act*. However, the existence of insolvency at the time, or as a result, of the conveyance is clearly a critical factor in impeaching virtually all conveyances: if the debtor was solvent at the date of the conveyance, and was not rendered insolvent by it, creditors would not be prejudiced, even where less than fair or adequate consideration was given. While the abolition of the requirement to prove insolvency might well preclude many of the technical squabbles concerning the precise meaning of the term, plaintiffs nonetheless would be faced with the requirement of proving that the conveyance injured creditors – that is, in most cases, proving both the absence of adequate consideration and what amounts to the insolvency or resulting insolvency of the debtor.

With respect to the proof of fraudulent intent, the proposals in the New Brunswick Report would, however, ease the plight of an impeaching creditor in several significant ways. For example, the Report recommended the abolition of the doctrine of pressure in all cases, and further proposed that, "if there is an intent to defeat creditors in a transaction, the transaction is voidable whether or not the intent to defeat creditors is the dominant intent".[319]

The extent to which the proposed new legislation would codify the several presumptions and inferences of fraudulent intent is unclear, particularly in view of the recommendation, reproduced above, that "the main principles of the judicial interpretation of the existing legislation" should be enshrined in the new statute. Only one such presumption was expressly made the subject of a recommendation:[320]

> It is recommended that there be a *prima facie* presumption of intent to defeat a particular creditor where a transaction is made after notice of the institution or intended institution of legal proceedings against the debtor by the creditor unless the creditor's claim is satisfied in full by the transaction or he consents to the transaction, or unless the transaction is made in accordance with procedures provided by law for the orderly payment of all creditors.

Essentially, this recommendation codifies, in part at least, the case law to the effect that a conveyance made pending a lawsuit is a badge of fraud.

A further proposal that would facilitate the impeachment of fraudulent transactions concerns what we have called the doctrine of concurrent intent. The Report recommended that, "subject to the express exemptions, if the intention of the debtor is to defeat creditors, the transaction is voidable whether or not the other party to that transaction concurred in that intent".[321]

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[319] New Brunswick Report, *supra*, note 30, at 156.

[320] *Ibid.*, at 155.

It will be recalled that, according to the New Brunswick Report, notice or knowledge of the debtor's intent on the part of the transferee is not sufficient to make the transaction voidable, notwithstanding the express language of 13 Eliz., c. 5; the transferee must concur in that intent. Unfortunately, it is not entirely clear from the discussion in the New Brunswick Report whether the proposal is designed solely to abolish the judicial gloss that requires concurrence of intent, or to abolish both the "notice or knowledge" requirement and the judicial gloss.

Turning next to the protection of certain transactions, reference should be made to several recommendations akin to the saving clauses in the Ontario *Assignments and Preferences Act*. The main recommendation was as follows:[322]

> It is recommended that the exemption for *bona fide* transactions, including the giving of security, be revised to cover only transactions in which both of the following conditions are met:
>
> (1) the consideration flowing to the debtor bears a fair and reasonable relative value to the consideration flowing from the debtor, and
>
> (2) the other party acts *bona fide* and without notice of either the intent of the debtor to defeat creditors or facts giving rise to a *prima facie* presumption of such an intention;
>
> and that provision for substituting one security for another be included within the exemption.

It should be noted that the proposal bears a very strong resemblance to the exceptions contained in a portion of section 5 of the Ontario *Assignments and Preferences Act*. However, the proposal does not conform to the exceptions in the *Fraudulent Conveyances Act*. Under that Act, a *bona fide* conveyance to an innocent third party may be saved where there is "good" or "valuable" consideration. In other words, it would be more difficult to save a transaction under the New Brunswick recommendation than under the *Fraudulent Conveyances Act*.

Paragraph (2) of the above recommendation also deserves some comment. Notwithstanding the abolition of the concurrent intent doctrine in an earlier proposal, this recommendation makes relevant the transferee's notice, albeit in conjunction with an absence of fair and reasonable consideration. In addition, one might ask again[323] what is the precise difference between, on the one hand, the transferee acting *bona fide* and, on the other hand, the transferee being either without notice of the debtor's fraudulent intent or without notice of the "facts giving rise to a *prima facie* presumption of such an intention". Could a transferee with such notice ever be *bona fide*? What matters other than notice are comprehended by the term "*bona fide*"?

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[321] *Ibid.*, at 156. It will be recalled that the doctrine of concurrent intent has been abolished by s. 2(5) of the *Frauds on Creditors Act*, R.S.P.E.I. 1974, c. F-13. See *supra*, this ch., sec. 4(a)(ii).

[322] New Brunswick Report, *supra*, note 30, at 157-58.

[323] See *supra*, this ch., sec. 2(b)(iv)a.

Aside from a proposal to preserve the "exemption for a security for a pre-existing debt and a present advance to enable the debtor to continue in business",[324] and "to protect a subsequent *bona fide* purchaser for value, without notice of the voidability of the transaction between the debtor and the other party, similar in effect to section 6 of the English statute",[325] the only other recommendation respecting statutory exceptions was for "any arrangement to pay an unsecured creditor entitled by law to priority over other unsecured creditors to the extent of the priority, with a reference relating, but not limiting, the exemption to statutory priorities such as that created by the *Wage-Earners Protection Act*".[326] This recommendation would expand upon the wage earners' exemption in what in Ontario is section 5(5)(*a*) of the *Assignments and Preferences Act*.

Before leaving transactions protected under the New Brunswick proposals, reference should be made to conveyances of exempt property. Here the Report partly reaffirmed existing law, but with a significant proviso. The recommendation read as follows:[327]

> It is recommended that an express exemption from the legislation be made for

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[324] New Brunswick Report, *supra*, note 30, at 158. It should be noted that s. 5(5)(*d*) of the *Assignments and Preferences Act*, the Ontario provision akin to the one referred to in this proposal, does not require that the "security given to a creditor for a pre-existing debt" should bear a fair and reasonable relative value to the advance made by the creditor. (See *supra*, this ch., sec. 3(d)(iv)d.(3).) Consequently, the value of the security could far exceed the amount of the advance. However, must the New Brunswick recommendation be read subject to the more general recommendation dealing with "the exemption for *bona fide* transactions, including the giving of security"? The latter recommendation provides, *inter alia*, that "the consideration flowing to the debtor [must bear] a fair and reasonable relative value to the consideration flowing from the debtor". If the recommendation respecting the giving of security in exchange for a present advance must be read subject to the more general recommendation, then there would be a statutory limit to the amount of security that could be given up by the debtor in exchange for an advance of money. However, the recommendation respecting the giving up of security is to the effect that the express exemption should be "continued", so that it is possible that no requirement of equivalence was intended.

[325] New Brunswick Report, *supra*, note 30, at 161. The New Brunswick Report contended (*ibid*., at 115, *n*. 139) that the "saving clause of the English statute would seem to refer, not to the transaction between the debtor and the third party, but to some subsequent transaction by the third party". It bears emphasizing, however, that the word "void" has been interpreted to mean voidable, and not void *ab initio*: see *supra*, this ch., sec. 2(b)(i). Commenting on the ambit of s. 172(3) of the English *Law of Property Act 1925*, c. 20, (akin to s. 3 of the Ontario *Fraudulent Conveyances Act* and s. 6 of 13 Eliz., c. 5), *Halsbury's Laws of England* stated that "the conveyance in question may be either the original conveyance by the debtor, or some subsequent conveyance made by the other party to the original conveyance or someone deriving title through him": (4th ed., 1977), Vol. 18, at 174, para. 371. The editors further stated that "[t]his rests upon the principle that the conveyance by the debtor is good until avoided": *ibid*., at 174, para. 371, *n*. 7.

[326] New Brunswick Report, *supra*, note 30, at 158.

[327] *Ibid*., at 157.

> any transaction in so far as it involves property which is exempt from execution, but that, where such a transaction would be voidable if the property were not exempt from execution, and to the extent that the consideration flowing to the debtor does not bear a fair and reasonable relative value to the consideration flowing from the debtor, any property transferred by the debtor be treated as remaining his property for the purpose of determining what property is exempt from execution and the debtor be treated as having selected such property to be exempt in any case where the debtor is entitled to select the property to be exempt.[328]

After considering transactions that ought not to be impeachable, the New Brunswick Report turned its attention to the unenviable position of most transferees for value subsequent to the voiding of a conveyance of property to them.[329] To ameliorate the harsh rules precluding compensation of such transferees, the Report put forth a proposal that would entitle a transferee for "valuable" consideration "to the return of any consideration he transferred to the debtor, whether as a release of security or otherwise, or its value and to set off this claim against any claim arising out of the setting aside of the transaction".[330] However, where the transferee "deliberately encouraged or assisted the debtor in furthering his intention to defeat creditors", his "claim is postponed until all other creditors existing when the transaction is set aside are satisfied in full".[331] In the latter case, it is not likely that the transferee would get his money back, since all the creditors must first be paid in full. Where the debtor is insolvent – a not infrequent phenomenon in this kind of case – creditors' claims could not be satisfied fully.

After dealing with the issue of standing[332] and the position of non-judgment creditors seeking to impeach a transaction,[333] the New Brunswick Report turned its attention to the recovery of property or proceeds subsequent to an invalidation of the transaction. The relevant proposals are as follows:[334]

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[328] Let us assume a $2,000 statutory exemption in respect of certain goods and that the debtor has two items in this class, each worth $2,000. He fraudulently conveys one of the items for $500 and then claims the remaining piece as his $2,000 exemption. While today the $500 proceeds are exigible, a $1,500 loss would be borne by the creditors. However, under the above recommendation, the piece sold at less than "fair and reasonable relative value" would be treated as remaining the debtor's property in order to determine what property is exempt; in other words, the debtor would retain the $500 proceeds, bear the $1,500 loss – this would constitute his $2,000 exemption – and the other $2,000 item would be exigible on behalf of the creditors.

[329] See *supra*, this ch., sec. 2(b)(vii)b. With respect to the rights of a transferee who has given up valuable security in exchange for payment to him by the debtor, see the Ontario *Assignments and Preferences Act*, *supra*, note 2, ss. 5(4) and 5(5)(*b*), discussed *supra*, this ch., sec. 3(d)(iv)d.(1).

[330] New Brunswick Report, *supra*, note 30, at 158-59.

[331] *Ibid.*, at 159. Presumably, a distinction was made between a transferee who "deliberately encouraged or assisted the debtor in furthering his intention to defeat creditors" and, for example, a transferee who (pursuant to the main recommendation protecting certain kinds of transactions) merely had "notice of either the intent of the debtor to defeat creditors or facts giving rise to a *prima facie* presumption of such an intention".

It should be noted that neither s. 5(4) nor s. 5(5)(*b*) of the Ontario *Assignments and Preferences Act* goes as far as the New Brunswick proposal. However, the provisions of s. 169(4)(*c*) and (5) of Bill C-12, *supra*, note 8, are more flexible with respect to the jurisdiction of a court to "restore each party to the transfer in so far as possible to the state that he was in immediately prior to the transfer".

[332] The New Brunswick Report recommended (*supra*, note 30, at 159-60) that "the person authorized to apply to have a transaction set aside be the sheriff when an execution is in his hands", so long as security for costs is first provided, although "provision [should] be made for a judgment creditor to obtain leave to take proceedings to have a

> It is recommended that the existing provision be continued for recovering from the person to whom the conveyance or preference is given either the property transferred to him by the debtor or, if he has disposed of the property, the proceeds of the property if they are still in his possession, and proceeds be defined to include any insurance moneys received on account of loss or damage to the property.
>
> It is recommended that provision be made, in the case of a person who deliberately encouraged or assisted the debtor in furthering his intention to defeat creditors, for recovering from such person, either the property transferred to him by the debtor or, if he has disposed of the property, the value of the property at the time it was transferred to him.

The existing provision referred to in the first recommendation reproduced above is section 21 of the New Brunswick *Assignments and Preferences Act*.[335] This provision, which is to be "continued" in the proposed new legislation, provides as follows:

> 21. If the person, to whom has been made any gift, conveyance, assignment,

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transaction set aside if there is no execution in the sheriff's hands, other than an execution issued by the creditor applying for leave" (*ibid.*, at 160). Unfortunately, the Report does not provide a rationale for this rather substantial change in the law with respect to *locus standi*.

The Report also recommended (*ibid.*, at 159) that "a summary procedure be provided for having a transaction which is voidable under the new legislation set aside by an application to a County Court judge or a Supreme Court judge, depending upon which Court would have jursidiction if the transaction were a matter in dispute in any ordinary civil action". However, it is not explained why, in another proposal, the Report recommended that a non-judgment creditor with standing to impugn a transaction must proceed by way of "an action by writ of summons" (*ibid.*, at 160), while a "summary procedure" was proposed in other cases.

In connection with a simplified procedure for attacking fraudulent transactions, reference should be made to ss. 9 and 10 of the British Columbia *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143, and r. 383(1) of the Alberta Supreme Court Rules, Alta. Reg. 390/68.

[333] Where the successful plaintiff is a non-judgment creditor, it was recognized that judgment would first have to be obtained before he could share in any distribution in respect of enforcement proceedings against the property the conveyance of which had been set aside; during this interval, the transferee "might have ample opportunity to dispose of the property and the proceeds" (New Brunswick Report, *supra*, note 30, at 146-47, *n*. 216). To prevent such a disposition, the Report recommended (*ibid.*, at 160) giving the court power "to make an order restraining disposition of the property by the person to whom it was transferred by the debtor until a reasonable opportunity is given to the creditor to obtain judgment against the debtor". With respect to the granting of injunctions in the context of fraudulent conveyance actions, see, for example, *Robert Reiser & Co., Inc. v. Nadore Food Processing Equipment Ltd.* (1977), 17 O.R. (2d) 717, 81 D.L.R. (3d) 278 (H.C.J.), and *City of Toronto v. McIntosh* (1977), 16 O.R. (2d) 257 (H.C.J.).

[334] New Brunswick Report, *supra*, note 30, at 160-61.

[335] R.S.N.B. 1973, c. A-16.

> transfer, delivery or payment, as in section 2 is mentioned, has sold or disposed of the property that was the subject of the gift, conveyance, assignment, transfer, delivery or payment, or any part thereof, the money or other proceeds realized therefor may be seized and recovered in an action under section 20 as fully and effectually as the property, if still remaining in the possession or control of such person, could have been seized or recovered.

It bears emphasizing that the first recommendation is, in one respect, rather narrow in scope, for it permits the tracing of proceeds only so long as they are "still in his [the transferee's] possession". Two points ought to be made in respect of this limitation. First, it appears that it is based on what we believe to be an erroneous interpretation of section 21. We are of the view that section 21 does not require the proceeds to be in the transferee's possession or control in order for them to be recovered.[336]

Secondly, with respect to section 21, it may be asked whether a transferee who, for example, deposits the proceeds in a bank still has the proceeds in his possession. The New Brunswick Report indicated that the answer likely would be in the negative, since it stated that, "[i]f the proceeds are mixed with other property in a way that they cannot be distinguished, they cannot be followed".[337] In other words, since the "existing provision" – that is, section 21 – is to "be continued", it would appear that proceeds that are commingled could not be traced under the New Brunswick proposal.

With respect to insurance proceeds, reference again should be made to the case law precluding the tracing of insurance proceeds arising from the loss, damage, or destruction of property transferred in fraud of creditors.[338] However, it bears emphasizing that the creditors could have seized the property itself from the transferee if it had not been lost, damaged, or destroyed, a fact that presumably animated the New Brunswick proposal.[339] It should also be noted that, in the context of the seizure of personal property, the Commission has recommended that insurance and other similar proceeds ought to stand in the place of exigible or exempt personal property.[340]

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[336] The New Brunswick Report stated that, under existing law, the "proceeds can only be followed as long as they remain 'in the possession or control' of the transferee": see *supra*, note 30, at 136. The emphasis of the quoted phrase "in the possession or control", and the absence of any authority for the above proposition other than an invocation of section 21, imply that it is section 21 that requires that the proceeds must remain "in the possession or control" of the transferee. However, it appears that this phrase has been taken out of context. Section 21 simply provides that the proceeds may be seized and recovered to the same extent as the property itself could have been seized if, of course, the *property* had remained "in the possession or control" of the transferee.

[337] *Ibid.*, at 136-37. The Report cited *J.R. Watkins Medical Co. v. Gray*, *supra*, note 187. See discussion *supra*, this ch., sec. 2(b)(vii)a. It also stated (at 137, *n*. 191) that "[t]he same applies under the English statute, if the proceeds can be followed at all: *Tennant & Co. v. Tallow* (1894), 25 O.R. 56 (Ch.)".

[338] See *supra*, this ch., sec. 2(b)(vii)a.

[339] Reference also should be made to the recommendation making a fraudulent transferee liable for the "value" of the property "if he has disposed of the property". However, what if the property were lost or destroyed?

[340] See Commission Report, *supra*, note 315, Part II, at 24-25, 88-89, and 184-87.

(b) RECOMMENDATIONS FOR REFORM UNDER THE PROPOSED NEW ENFORCEMENT REGIME

As indicated earlier, the New Brunswick Report contained two sets of recommendations, the first based on retention of the present enforcement system, the second as part of a more comprehensive reform. In the latter context, the New Brunswick Report proposed the adoption of a completely different type of enforcement regime in which a new enforcement office would be given broad supervisory powers over almost all aspects of judgment debt enforcement.[341] In respect of voidable transactions under the proposed new enforcement regime, the Report stated, in part, as follows:[342]

> The best mechanism for protecting innocent third parties while binding property in the hands of the debtor lies in the provisions for setting aside transactions made with intent to defeat creditors that were recommended in the discussion of the existing system. In those recommendations a *prima facie* presumption of intent to defeat creditors was proposed in the case of any transaction by a debtor after commencement of a legal action. When enforcement proceedings [that is, under the proposed new regime] are commenced, it is proposed that a similar, but irrebuttable, presumption apply to any transaction by a debtor between service of a notice of enforcement and service of the enforcement decision and to any transaction made after service of the enforcement decision which is contrary to that decision.

The above proposals add little to those recommended in the context of the existing regime, all of which would be incorporated into the new system.[343] The only addition is the proposal that there should be an irrebuttable presumption of intent to defeat creditors in the event of a transaction by a debtor "between service of a notice of enforcement and service of the enforcement decision [as recommended in the Report] and . . . any transaction made after service of the enforcement decision which is contrary to that decision". One may well question the focus of this proposal. It appears to be theoretically possible for a conveyance to be avoided under the proposal where the debtor was solvent at the time of the conveyance and where full consideration was received, so that creditors would not in fact be prejudiced. Of course, in many cases the proposed exception in respect of good faith transferees would save the transaction, although this manner of saving a transaction seems unnecessarily oblique in light of what we believe to be the fundamental objective of voidable transactions legislation – that is, the invalidation of transactions that actually prejudice creditors.

6. REFORM OF THE PRESENT LAW

The preceding sections of this chapter have examined the existing law respecting voidable transactions, the deficiencies and ambiguities with respect to that law, legislation in other jurisdictions, and proposals for reform recommended in New Brunswick. It is clear that both the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act* are, in many areas, only skeletal in form; consequently, it has been left to the courts to decipher often inadequate legislation and to delineate its precise scope. This encrustation of a massive amount of case law has not been entirely satisfactory. For example, to some degree it has served to emasculate what at first blush appears to be the very foundations of the legislation. This kind of distortion of the express statutory requirement to prove a debtor's fraudulent intent may, in turn, have given rise to a somewhat myopic view of that requirement – a view that perceives the need to prove subjective fraudulent intent as an almost insurmountable obstacle. Indeed, this misperception – which largely ignores the means of proving fraudulent intent by the marshalling of objective facts – may well inhibit the institution of actions under provincial legislation.

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[341] This regime is described in Commission Report, *supra*, note 315, Part I, at 107-09.

[342] New Brunswick Report, *supra*, note 30, at 284.

[343] *Ibid.*, at 284-85.

It is clear from the jurisprudence that courts have been more than willing to employ presumptions and inferences to aid a plaintiff seeking to avoid a fraudulent transaction. The presumption of fraudulent intent arising from a transaction that has the effect of defeating creditors may no longer be irrebuttable in law; however, the use of even a rebuttable presumption is itself highly significant, since it places the burden of adducing explanatory evidence squarely on the defendant. Where the debtor was insolvent at the time of the transaction, or rendered insolvent by it, and where the transaction was a gift or for only nominal consideration, the courts have had little difficulty in voiding the transaction. While due attention is, of course, paid to fraudulent intent, its presence is often noted only by way of lip-service to the statute; normally, it is the natural effect of the transaction, and not evidence of subjective intent, that has primarily animated the court's view of the proper course of action.

Examination of existing and proposed fraudulent conveyance legislation in various jurisdictions makes it clear that, while there indeed are many technicalities that must be considered in formulating recommendations for reform, the choice of the general governing regime is essentially a matter of policy. The central issue that forms the main boundary within which the choice must be made is the extent to which the legislation respecting voidable transactions ought to protect creditors, irrespective of the fraudulent intent of the debtor or transferee. This issue involves a consideration of the extent to which the legislation ought to reflect commercial practice and expectations and not impede normal commercial activity.

Insofar as preferences to creditors are concerned, the Commission has had to bear in mind its proposals for new creditors' relief legislation.[344] Most importantly, it is clear that our reaffirmation of the principle of equality enshrined in the *Creditors' Relief Act* necessarily requires a close scrutiny of all preferences. Indiscriminate and unregulated preferences cannot be countenanced in any regime in which unjustified priorities among creditors are sought to be precluded. Given, then, this need for adequate preference legislation, we are again faced – as in the case of fraudulent conveyances – with the fundamental issue described above.

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[344] See the forthcoming Part V of the Commission's *Report on the Enforcement of Judgment Debts and Related Matters*.

The Commission has had no difficulty coming to the conclusion that the law in respect of voidable transactions is in need of reform. Accordingly, we recommend the repeal of the provisions of the *Fraudulent Conveyances Act* dealing with conveyances in fraud of creditors and the provisions of the *Assignments and Preferences Act* dealing with fraudulent conveyances and fraudulent preferences. Further, we recommend that a single new statute should be enacted in their place. In setting forth our recommendations for new legislation in the pages that follow, we have been animated by a twofold purpose: first, to ensure that creditors are afforded adequate remedies in order to satisfy their legitimate debts – and, more particularly, to preclude the unwarranted dissipation of a debtor's exigible assets – and, secondly, to protect reasonable commercial and non-commercial dispositions of property.

(a) RECOMMENDATIONS FOR REFORM: FRAUDULENT CONVEYANCES

(i) The General Rule

Without doubt, the most difficult and controversial issue in respect of fraudulent conveyances concerns the jurisdictional fact or facts upon which an attack on a conveyance may be founded. The Commission has carefully weighed the critical policy issue, namely, whether the law should focus on the protection of creditors where a conveyance does in fact prejudice their ability to satisfy their debts, or whether the law should continue to be premised on, and therefore punish, the nefarious behaviour of debtors, irrespective of the effect of the transaction in question. Should the civil law have any concern with a debtor's fraudulent intent where no one has been injured? And, conversely, should creditors be left without a remedy where, in spite of prejudice to them, the debtor cannot be shown to have had any fraudulent intent?

On balance, we are of the view that, to focus attention in the legislation on the intent of the debtor, insofar as this activity requires investigation and analysis of purely subjective factors, is to distort what we believe should be the essential purpose of fraudulent conveyance legislation – that is, the invalidating of transactions that in fact prejudice the debtor's creditors. In this regard, we fully endorse the famous aphorism of Lord Hatherley L.C., in *Freeman v. Pope*,[345] that "[t]he principle on which [fraudulent conveyances legislation] proceeds is this, that persons must be just before they are generous, and that debts must be paid before gifts can be made". However meritorious or well-intentioned the debtor's conveyance may be, we believe that, aside from certain protected transactions to which reference will be made below, it must perforce give way to the higher claims of the debtor's legitimate creditors. Moreover, to continue in so many cases to pay lip-service to the requirement of proving fraudulent intent on the part of the debtor, while at the same time necessarily concentrating on more objective criteria, such as the effect of the conveyance, and employing a plethora of presumptions and inferences to supplement the inevitable paucity of evidence concerning actual intent, is an attempt to do indirectly that which should be done directly. We are of the opinion, as were the

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[345] *Supra*, note 51, at 540.

American Uniform Law Commissioners, that such presumptions and inferences of fraudulent intent have been employed to an unwarranted degree, notwithstanding their invocation as a means of doing justice in individual situations.[346] We believe that the ends of justice can best be served by recognizing explicitly the centrality of the general principle that conveyances prejudicial to creditors ought not to stand.

The abandonment of a regime based on fraudulent intent for a regime focusing on the effect of a conveyance on the debtor's ability to pay his creditors is not as radical a step as might appear. In the first place, generally speaking,[347] the law of debtor and creditor is not concerned with a debtor's intent in ensuring that his assets are made available to creditors. This fact is clearly reflected in the Commission's recommendations respecting, for example, the seizure and sale of personal property,[348] garnishment of income and other debts,[349] and equitable execution.[350] Secondly, the criminal law deals with the disposition, gift, conveyance, assignment, sale, transfer, or delivery of property by a person who intends to defraud his creditors thereby,[351] punishing what have been characterized as criminal acts by fraudulent debtors. These efforts need not be duplicated by the Province. Thirdly, notwithstanding the restrictions generally, although not universally, placed by the more modern case law on the *Freeman v. Pope* doctrine – a doctrine legitimizing a type of regime based on the effect of a conveyance – the continued use of presumptions and inferences in respect of a debtor's intent has made it considerably easier to espouse the cause of such a regime: the adoption of a regime based on the effect of the impugned transaction will, in the main, merely codify and render unambiguous the essential thrust of existing law. Indeed, the majority of the cases concern conveyances by an insolvent debtor for no consideration or only nominal consideration, that is, conveyances that in fact prejudice creditors. Where a conveyance does not have this effect, but where the debtor nonetheless intended to prejudice creditors, the law ought not to intervene in order to punish the offending debtor for his dishonourable conduct. As expressed above, the exclusive purpose of provincial fraudulent conveyances legislation should be the protection of creditors.

Finally, it bears emphasizing that, notwithstanding the historical roots of a regime based on fraudulent intent, there are statutory precedents for the adoption of a regime premised on the effect of the transaction in question. It will be recalled, for example, that section 4 of the American Uniform Fraudulent Conveyance Act invalidates a conveyance on the basis that it has prejudiced creditors – irrespective of the debtor's intent – since it deals with a conveyance for less than fair consideration by a debtor who was insolvent at the date of the conveyance or who was rendered insolvent by it.[352] The existence in the Uniform Act of section 7, a provision focusing on the debtor's intent, in no way detracts from the importance and efficacy of section 4 as a completely independent section manifesting a philosophy espoused earlier in this section by the Commission.

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[346] See text supporting note 307, *supra*.

[347] An exception is prejudgment relief, discussed *supra*, ch. 2.

[348] See Commission Report, *supra*, note 315, Part II, ch. 2.

[349] See *ibid.*, ch. 3.

[350] See *ibid.*, ch. 4.

[351] See *Criminal Code*, R.S.C. 1970, c. C-34, s. 350(*a*).

[352] There also are examples of legislation focusing only on the effect of a transaction in

Having regard, therefore, to the general policy of protecting creditors against the unwarranted disposition of exigible assets by debtors, the existing case law, including the considerable array of presumptions and inferences respecting intent, present sanctions in the criminal law for fraudulent dealing with property, and statutory precedents for voidable transactions regimes not premised on fraudulent intent, the majority of the Commission is of the opinion that the existing basis for impeaching a fraudulent conveyance ought to be changed. Accordingly, a majority of the Commission recommends that, as a general principle and subject to the provisions proposed below, a creditor should be entitled to have a conveyance by a debtor to a third party (not being a creditor) set aside where the effect of the conveyance was to defeat, hinder, delay, or defraud one or more of the debtor's creditors.[353]

(ii) The Definition of "Conveyance"

Section 1(*a*) of the *Fraudulent Conveyances Act* provides that the term "conveyance" "includes gift, grant, alienation, bargain, charge, encumbrance, limitation of use or uses of, in, to or out of real property or personal property by writing or otherwise". Section 4(1) of the *Assignments and Preferences Act* includes the phrase "assignment or transfer, delivery over or payment". Section 2(a) of the Newfoundland *Fraudulent Conveyances Act* also comprehends in its definition of "conveyance" a "transfer,

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the context of preferences to creditors. For example, s. 42 of the Manitoba *Assignments Act*, R.S.M. 1970, c. A150, invalidates conveyances to creditors within 60 days of the conveyance if the effect is to give the creditor a preference over other creditors. The intent of the debtor and preferred creditor, as well as any pressure brought to bear on the debtor and any want of notice of the debtor's fraudulent intent on the part of the creditor, are all irrelevant. See discussion *supra*, this ch., sec. 4(a)(v).

[353] Dissent by the Chairman, Dr. D. Mendes da Costa:

> Under the present law, the party seeking to impugn a transaction must establish a fraudulent intent. As I read the cases, the intent requirement, itself, has not been the focus of criticism; rather, the courts have pointed to the difficulties involved in the proof of intent. I share my colleagues' view that the present situation is in need of reform, but I do not agree that an "effect regime", as proposed by my colleagues, is the appropriate response. In my view, such a regime would place the courts in a very rigid position: once the party seeking to impugn the transaction has established the required effect, the court would have no option but to set the transaction aside, unless the proposed protective provision was to apply (see *infra*, this ch., sec. 6(a)(vi)). Intent would be utterly irrelevant. Nor would it matter that insolvency was marginal or of a temporary nature. (In this connection, reference should be made to section 179 of Bill C-12, *supra*, note 8, which would protect a transaction where, at any time after such transaction and before the date of bankruptcy, "the person who subsequently became a bankrupt was solvent".) As with any rigid system, there could be no certainty that the result of the regime proposed by the majority of the Commission would always be in the best interest of justice. I would support a more flexible approach, one that would sweep away the present presumptions of fraud. In my opinion, proof of prejudicial effect should operate to shift the onus of proof to the grantee; it should, however, be open to a grantee, who seeks to preserve a transaction, to prove that it was not made with the intent to defeat creditors.

assignment, delivery over, [or] payment . . .". Section 1 of the United States Uniform Fraudulent Conveyance Act defines "conveyance" to include "every payment of money, assignment, release, transfer, lease, mortgage or pledge of tangible or intangible property, and also the creation of any lien or incumbrance".

The definition of "conveyance" in the *Fraudulent Conveyances Act* and the enumeration of transactions comprehended by section 4(1) of the *Assignments and Preferences Act* have not caused difficulties in the past, particularly since, in the former case, section 1(*a*) simply lists certain types of disposition as examples of conveyances; the definition by its terms is not intended to be exhaustive. However, in view of our purpose to recommend entirely new legislation, the Commission believes that a more expansive definition of the term "conveyance" ought to be adopted. Accordingly, we recommend that, for the purposes of the new legislation proposed in respect of fraudulent conveyances, the term "conveyance" should be defined to include a gift, transfer, grant, assignment, alienation, bargain, delivery over, lease, charge, mortgage, encumbrance, payment, release, limitation of use or uses, and any other type of disposition of, in, to, or out of any right, title, or interest in real property or personal property of any kind, whether by writing or otherwise.

The reason for the addition in our proposal of most of the new terms to the existing definition in the *Fraudulent Conveyances Act* is to make the new definition more comprehensive.[354] However, we do wish to mention the reference to personal property "of any kind". In this connection, we do not believe that the new legislation should be invocable only where, for example, tangible personal property has been conveyed. One case where the Court gave a broad interpretation to the existing legislation is *Re Geraci*.[355] In that case, the Court of Appeal, reversing the lower court decision,[356] stated by way of *obiter dictum* that the designation of a beneficiary of a life insurance policy under *The Insurance Act*[357] fell within the definition of "conveyance" under *The Fraudulent Conveyances Act* and, therefore, could be set aside against creditors of the insured. In our view, the matter should be put beyond doubt. Moreover, by making reference to "any right, title, or interest" in real or personal property, the Commission intends to include any legal, equitable, or partial right, title, or interest.

(iii) The Determination of the Effect of a Conveyance

With respect to possible legislation relating to the manner in which the effect of a conveyance may be determined, the Commission has considered two basic options. First, the Commission's fundamental recommendation to create a regime premised on the effect of a conveyance could be regarded as sufficient; in other words, new legislation would not particularize the factors that the court should consider when determining the effect of an impeached conveyance. Proponents of this option might argue that the factors to which the court should make reference – for example, the debtor's financial status and the consideration received – are self-evident and need not be specified. The second option would give more guidance to the court, for example, by stipulating the conditions under which a conveyance should be set aside.

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[354] In view of the Commission's recommended definition of "conveyance", it may not be necessary to define separately the terms "personal property" and "real property". See, now, s. 1(*b*) and (*c*) of the *Fraudulent Conveyances Act*.

[355] [1970] 3 O.R. 49 (C.A.).

[356] (1969), 13 C.B.R. (N.S.) 86 (Ont. S.C. in Bktcy.).

[357] R.S.O. 1970, c. 224. See, now, R.S.O. 1980, c. 218.

At present, legislation in some jurisdictions that have adopted a form of "effect" test in respect of fraudulent conveyances has not specified the means by which the effect of a conveyance is to be determined by the court. For example, article 1033 of the Quebec *Civil Code* provides in part only that a "contract cannot be avoided unless it . . . will have the effect of injuring the creditor". Similarly, section 169(5) of Bill C-12 refers simply to the situation where the court finds that "the effect of the transfer was to impede, obstruct, delay or defraud the creditors or any of them". In other cases, specific factors are isolated. For example, section 4 of the United States Uniform Fraudulent Conveyance Act provides that "[e]very conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration". The statutory definitions of "insolvency" and "fair consideration" in sections 2(1) and 3, respectively, make unambiguous the ingredients of the "effect" regime manifested in section 4.

The debtor's financial status and the consideration received for the conveyance are clearly central to a determination of the effect of a conveyance on the debtor's ability to pay his creditors. Turning first to the debtor's financial position, a debtor who is insolvent at the date of the conveyance, or who is rendered insolvent thereby, and who, as we shall see, receives inadequate consideration,[358] obviously has prejudiced his creditors by the conveyance. Notwithstanding the importance of the debtor's financial status, however, it is arguable that it is not strictly necessary to mention such specific factors in legislation reflecting a regime based on the effect of a conveyance. Clearly, a creditor seeking to attack a conveyance necessarily must have regard to the debtor's financial position both before and after the conveyance. He may find that the debtor had an excess of liabilities over exigible assets; or he may find that the debtor has been unable to meet his obligations as they become due. Irrespective of whether proof of "insolvency" is an express statutory requirement, an impeaching creditor inevitably must use either of these two methods of indicating that creditors have suffered because of the conveyance.

The second critical ingredient of a regime based on the effect of a conveyance is the consideration paid to the debtor for the conveyed property. As in the case of the debtor's financial status, it may be argued that little is to be gained by defining or specifying the extent of the consideration required to be given to save a conveyance. An impeaching creditor clearly must have regard to the factor of consideration in assessing the effect of the conveyance.

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[358] See Walden, "Creditors' Rights: Conveyances in Fraud of Subsequent Creditors" (1952), 40 Ky. L. J. 433, at 434-35.

At present, courts are provided with statutory guidance with respect to the matter of consideration. For example, sections 3 and 4 of the *Fraudulent Conveyances Act* require, respectively, good and valuable consideration. Other statutes, however, provide what we consider to be more suitable standards. Section 5(1) of the Ontario *Assignments and Preferences Act* requires that the "goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor". Section 3(a) of the American Uniform Fraudulent Conveyance Act provides that "[f]air consideration is given for property, or obligation", *inter alia*, "(a) When in exchange for such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed . . .". The authors of the New Brunswick Report would exempt transactions in which two conditions are met, one of which is that "the consideration flowing to the debtor bears a fair and reasonable relative value to the consideration flowing from the debtor".

On balance, the Commission is of the opinion that courts should be provided with statutory guidance concerning what factors to consider when determining the effect of a conveyance on a debtor's creditors. Indeed, we believe that the new legislation should go even further: it should state uneqivocally that specified kinds of conveyance, which clearly prejudice creditors, must be set aside. Accordingly, we recommend that legislation should provide that a conveyance has the effect of defeating, hindering, delaying, or defrauding creditors where (a) the debtor was insolvent at the date of the conveyance or rendered insolvent by the conveyance, and (b) the consideration given for the property conveyed was not fair and reasonable relative to the value of such property.

Paragraphs (a) and (b) together clearly delimit one situation in which a court would be required to set aside a conveyance as having a prejudicial effect on creditors. However, it may well be the case that a conveyance made in other circumstances would have a similar effect. For example, in *Bott v. Smith*,[359] Sir John Romilly M.R. stated that, "[e]ven if full consideration had been given, that is not sufficient, because, as is shewn in the case in Atkins (*Stileman v. Ashdown*, 2 Atk. 477), the consideration may be given in such a form as to defeat the judgment creditor . . .". In a regime founded on the effect of a conveyance, the nature or form of the consideration, compared to the property conveyed, may well be a significant factor. Or, for example, a prejudicial conveyance may be made by a debtor who is technically solvent but whose assets, which are located outside Ontario, cannot readily be sold to cover all known or anticipated liabilities.

Accordingly, in order to permit flexibility so that creditors could have a conveyance set aside in all appropriate situations, we recommend that legislation should make it clear that proof of insolvency and lack of fair and reasonable consideration should not be the only means of establishing the prejudicial effect of a conveyance. The enumeration of such criteria should not restrict or limit the general applicability of the legislation creating the type of regime we propose, nor should it in any way circumscribe the right of a creditor to have a conveyance set aside in any case where the effect of the conveyance was to defeat, hinder, delay, or defraud one or more of the debtor's creditors.

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[359] (1856), 21 Beav. 511, at 517, 52 E.R. 957 (Rolls). See, also *Bank of Montreal v. Vandine*, *supra*, note 45, at 461-62.

A further question arises concerning the desirability of defining insolvency. If our proposed legislation were not to define the term "insolvent", arguably the interpretation of legal insolvency and commercial insolvency put forward by Rose J., in *Rae v. McDonald*,[360] would continue to apply as it has been applied in the past to cases under section 4(1) of the *Assignments and Preferences Act*.

The Commission has concluded that the term "insolvent" should be defined in the legislation. First, we believe that whatever confusion or ambiguity there is in the case law can easily be laid to rest – at least at the conceptual level – if there is reasonable specificity in the statute. Secondly, we do not wish to endorse the interpretation of insolvency given by Rose J. in *Rae v. McDonald*. Accordingly, the Commission recommends that, insofar as fraudulent conveyances are concerned, a person should be deemed to be insolvent where (a) he does not have sufficient property subject to enforcement measures to pay all his debts in full, if such property were sold at fair market value, rather than under legal process, or (b) he has ceased to pay his debts generally as they become due.

As stated above, while the majority of cases favour the "forced sale", rather than the "fair market value", method of valuation in respect of legal insolvency, the matter is by no means conclusively settled. Section 2 of the *Bankruptcy Act*, in defining "insolvent person", speaks in terms of both "a fair valuation" and "a fairly conducted sale under legal process". Bill C-12, section 4(*a*), refers to property "realized at a fair value". In defining "insolvency", section 2 of the Uniform Fraudulent Conveyance Act speaks of "the present fair saleable value" of the debtor's assets.

The Commission is of the view that the "fair market value" method is more reasonable for two reasons. First, it would likely produce greater certainty with respect to the valuation of a debtor's property, particularly in locales where there has been little experience in evaluating certain kinds of property at forced sales. Secondly, we believe that, in view of the Commission's proposal in favour of a regime based on the effect of a conveyance – thereby making it somewhat easier for a creditor to impeach a conveyance – the pendulum must not be swung too far. The new legislation must strike an equitable balance between the rights of creditors and debtors. Therefore, we have opted for a method of valuation more beneficial to debtors.

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[360] *Supra*, note 29. See discussion *supra*, this ch., sec. 2(b)(ii).

(iv) Entitlement to Attack a Conveyance: The Definition of "Creditor"

It will be recalled that the phrase "creditors or others" in section 2 of the *Fraudulent Conveyances Act* has been interpreted to give a broad range of claimants entitlement to sue. There are two main issues with respect to *locus standi* under the proposed new legislation. The first issue concerns whether only creditors existing at the date of the conveyance should have standing, or whether subsequent creditors, whose claims arise after the conveyance, also should be permitted to impeach it. The second issue concerns the definition of "existing creditors".

a. Creditors Existing at the Time of the Conveyance

Section 1 of the Uniform Fraudulent Conveyance Act defines "creditor" to be "a person having any claim, whether matured or unmatured, liquidated or unliquidated, absolute, fixed or contingent". The New Brunswick Report recommended that "creditor" should be "generally defined to include [*inter alia*] a person who has a cause of action against another person, without regard to whether the claim is liquidated or whether a judgment has been obtained on the cause of action . . .".

Clearly, a conveyance of property by a debtor may have the effect of defeating, for example, the claim of a person who, at the time of the conveyance, has a cause of action in tort against the debtor. Having regard to the existing provision in the *Fraudulent Conveyances Act*, and notwithstanding the restrictiveness of section 4(1) of the *Assignments and Preferences Act*, there is virtually universal agreement that fraudulent conveyances legislation ought not to countenance such a flagrant injustice. Accordingly, the Commission recommends that the term "creditor", as it relates to the entitlement to impeach a conveyance, should be defined broadly to mean a person who, at the time of the conveyance, has a judgment or cause of action against the debtor, whether the claim in respect of the cause of action is liquidated or unliquidated, absolute or contingent, certain or disputed, or payable immediately or at a future time. This recommendation would provide maximum protection to existing creditors, while still permitting defendants to challenge the legitimacy or validity of claims alleged by plaintiffs who are non-judgment creditors.[361]

b. Creditors Arising Subsequent to the Conveyance

We have seen that, under the *Fraudulent Conveyances Act*, a creditor whose judgment or cause of action arises subsequent to a conveyance may seek to impeach that conveyance only where: (a) there still remains unpaid a creditor whose judgment or cause of action existed at the date of the conveyance, except where, in order to pay his existing creditors, the debtor substitutes a subsequent creditor for them; (b) the debtor's intent was to defraud creditors generally, to defraud subsequent creditors generally, or to defraud the subsequent creditor seeking to impeach the conveyance; or (c) the debtor is engaged or is about to engage in a "hazardous" or "risky" business or undertaking and knows or ought to know that he will become indebted.[362] We have also seen that various cases allude to the difficulties in finding a solid basis for giving a subsequent creditor standing to impeach a conveyance made before his claim or cause of action arose. Some cases emphasize, for example, the unexpected nature of the debtor's subsequent insolvency. If the insolvency arose because of events that were unforeseen at the time of the conveyance, and if the subsequent debt arose a great length of time after the conveyance, the causal connection between the conveyance and the debtor's inability to meet the subsequent obligation is particularly difficult to demonstrate.[363] If a conveyance could be invalidated under these circumstances, would solvent persons and transferees have any certainty concerning the validity of a conveyance?

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[361] See, for example, the jurisdiction of a judge under r. 126 of the Supreme Court of Ontario Rules of Practice, R.R.O. 1980, Reg. 540, to strike out pleadings on the ground that they disclose no reasonable cause of action.

To date, of course, this problem has arisen only in the context of a regime based on fraudulent intent, but it clearly would be critical in a regime based on the effect of a conveyance.[364] With respect to the latter type of regime, and taking it to its logical extreme, one could argue that, so long as the claim of the subsequent creditor could have been satisfied by the conveyed property, but not without it, that creditor has in fact been prejudiced by the conveyance and should be entitled to have it set aside. Presumably, some would make this argument irrespective of the ordinary expectations of the debtor at the time of the conveyance; they would contend that the only critical issue is whether the effect of the conveyance was to limit the debtor's ability to pay the subsequent creditor, and not whether the debtor intended this effect or contemplated the likelihood of future creditors at the time of the conveyance.

The New Brunswick Report recommended "that the term 'creditor' be defined . . . to include . . . future creditors".[365] The Report further recommended the abolition of the present rule that subsequent creditors can sue only where existing creditors remain unpaid, or where the debtor has entered into a "hazardous" or "risky" business in which many creditors are expected and may not be paid, or where the debtor had an actual intention to defeat future creditors generally or a particular future creditor.[366] The American Uniform Fraudulent Conveyance Act also manifests concern over the plight of subsequent creditors; indeed, three separate sections – sections 5 to 7 – either deal generally with the issue or make reference to particular aspects of it.[367]

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[362] See discussion *supra*, this ch., sec. 2(b)(vi)a.(4).

[363] See, for example, *Mackay v. Douglas*, *supra*, note 57, at 121, and *Elgin Loan and Savings Co. v. Orchard*, *supra*, note 62, at 700. See, also, C.H.F., *supra*, note 162, at 674: "Where the grantor makes a voluntary conveyance with intent to defraud future creditors, the time that elapses between the conveyance and the creation of the debt ought to be considered to ascertain whether the conveyance injured the subsequent creditor."

[364] See Walden, *supra*, note 358, at 437:

> [O]nce the transaction is completed, it is much more difficult to connect it with some future liability. If the subsequent debt arose a great length of time afterward, the connection is especially difficult to show. Something must be found which justifies the statement that the debtor intended to injure the future creditors.

[365] New Brunswick Report, *supra*, note 30, at 154.

[366] See discussion *supra*, note 317.

From the foregoing discussion, it should be clear that the issue of standing in respect of subsequent creditors is not easy to resolve, either as a matter of policy or as a practical matter. On balance, however, a majority of the Commission has come to the conclusion, and accordingly recommends, that a creditor whose judgment or cause of action arose subsequent to a conveyance should not have a right to impeach that conveyance.[368]

In the first place, we are of the view that subsequent voluntary creditors cannot be heard to complain of their disentitlement, since they extended credit on the basis that the property comprehended by the conveyance no longer belonged to the debtor. We do acknowledge that it is mainly the large institutional lenders or other creditors similarly situated that have the means of investigating the debtor's financial circumstances before credit is extended. Clearly, some creditors either do not have ready access to credit information or, because of the financial burden, stiff competition, or some other reason, believe they cannot investigate every potential borrower. However, where for whatever reason no investigation is undertaken, and no security is demanded, creditors must be taken to have assumed a certain risk in doing business; in this respect, their potential loss as a result of a prior conveyance is no different than their potential loss because, for example, they have been involved in unsuccessful products liability litigation as a consequence of their unwillingness to establish an adequate product control procedure.

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[367] Sections 5-7 deal, respectively, with conveyances by persons in business, conveyances by persons about to incur debts, and conveyances made with intent to defraud.

[368] Dissent by the Honourable Richard A. Bell:

> If this recommendation were adopted, a significant existing right under the *Fraudulent Conveyances Act* would be abolished. The New Brunswick Report has recommended "that the term 'creditor' be defined . . . to include . . . future creditors". The American Uniform Fraudulent Conveyance Act also deals with "future" – that is, subsequent – creditors. The relevant sections of the latter statute provide as follows:
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> > 5. Every conveyance made without fair consideration when the person making it is engaged or is about to engage in a business or transaction for which the property remaining in his hands after the conveyance is an unreasonably small capital, is fraudulent as to creditors and as to other persons who become creditors during the continuance of such business or transaction without regard to his actual intent.
> >
> > 6. Every conveyance made and every obligation incurred without fair consideration when the person making the conveyance or entering into the obligation intends or believes that he will incur debts beyond his ability to pay as they mature, is fraudulent as to both present and future creditors.
>
> If the recommendation of the majority of the Commissioners is adopted, it would place Ontario law out of step with other jurisdictions.
>
> To deprive subsequent creditors entirely of a right to challenge a conveyance is an invitation to fraudulent persons to make themselves "judgment-proof" so that they can commit actionable wrongs, such as libel or slander, with impunity. Accordingly, ss. 5 and 6 of the American Uniform Fraudulent Conveyance Act should be adopted.

We now turn to consider the position of involuntary subsequent creditors – for example, tort claimants whose causes of action arose subsequent to the conveyance in question. Given the broad scope of our earlier proposal in respect of existing creditors entitled to impeach a conveyance, there would not likely be many situations where, as a matter of policy, an involuntary subsequent creditor reasonably should be given the right to sue. Ordinarily, one would have thought that, at the date of the conveyance, a person entitled to sue at least should have a cause of action, even if his claim is unliquidated, disputed, or contingent, if he properly ought to be comprehended by the legislation. If no such cause of action exists, we believe that the subsequent involuntary creditor must, in a sense, take his debtor as he finds him.

(v) The Doctrine of Concurrent Intent

Under the doctrine of concurrent intent, an impeaching creditor must prove that the transferee had "notice or knowledge" of the debtor's fraud, or, depending upon the interpretation of these terms, that he was a party to the fraud. In the absence of such proof, the creditor will not be able to have the conveyance set aside, at least where valuable consideration has been given. While, at present, the doctrine is woven inextricably into the fabric of the provincial statutes, it flies in the face of the type of regime recommended by the Commission. We have eschewed the concept of fraudulent intent and supplanted it with the fundamental principle that a creditor should be entitled to have a conveyance set aside where the effect of the conveyance was to defeat, hinder, delay, or defraud one or more of the debtor's creditors. Inasmuch as the doctrine of concurrent intent would not be relevant under the proposed new regime, we recommend that a conveyance should be voidable irrespective of the intent of the transferee.

(vi) Protected Conveyances

Fraudulent conveyance legislation commonly protects *bona fide* transferees for valuable consideration. With respect to *bona fides*, it is our view that the corollary of the abolition of the doctrine of concurrent intent, as proposed in the preceding section, is the abolition of the right of transferees to use their *bona fides* to support the validity of the transaction in question. With respect to the matter of consideration, it will be recalled that, while some statutes, such as the Ontario *Fraudulent Conveyances Act*, demand "good" or "valuable" consideration, other statutes require consideration that is "fair and reasonable" relative to the property conveyed. The Ontario *Assignments and Preferences Act* and the American Uniform Fraudulent Conveyance Act fall into the latter category, and this approach has been endorsed in the New Brunswick Report.

The Commission believes that the proposed new legislation should continue to protect certain transferees for value. The only issue that has caused us some concern is whether the saving clause should protect transferees for "valuable" consideration, for "good" consideration, or for "fair and reasonable" consideration. On balance, we have concluded that, in light of the basic purpose of fraudulent conveyance legislation – namely, to protect creditors from prejudicial conveyances – a stricter approach ought to be adopted. Accordingly, we recommend that the proposed legislation should contain a protective provision to the effect that a conveyance by a debtor should not be set aside where the consideration given for the property conveyed was fair and reasonable relative to the value of the property.[369] Where fair and reasonable consideration has been given, it can be said that the value of the debtor's asset pool has not been materially lessened to the detriment of his creditors.

Before leaving the issue of protected conveyances, it bears noting that we do not favour a separate saving provision in respect of goods sold in the ordinary course of business. Ordinarily, the consideration offered for goods sold in the normal course of business would bear a fair and reasonable value relative to the property conveyed; therefore, the transaction would be saved under the proposal made above. However, such goods may well be sold for a small fraction of their fair market value. To recommend an exception to the proposed "fair and reasonable" standard for goods sold in the normal course of business might well encourage a comprehensive liquidation of a merchant's inventory for a low cash consideration, preparatory to absconding from the jurisdiction. As indicated above, the very nature of the proposed new fraudulent conveyances regime, and the philosophy that underlies it, bespeak a fundamental concern to protect creditors with legitimate claims against their debtors – a protection that should be afforded, we believe, only where fair and reasonable consideration has been forthcoming.

(vii) The Doctrine of Pressure

Arguably, the doctrine of pressure is relevant, at least conceptually, in a regime founded on fraudulent intent: the transfer of property solely or mainly as a result of pressure from the transferee operates to negative the intent of the debtor to defraud his creditors. The doctrine of pressure also is related to the issue of the transferee's good faith, although the two matters are conceptually distinct. However, to the extent that the doctrine is now or ever was relevant in respect of fraudulent conveyances, it clearly would have no applicability in a regime based on the effect of a conveyance. Accordingly, we recommend that a conveyance should be voidable whether the conveyance is made voluntarily or under pressure.

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[369] In the vast majority of cases, the prejudicial effect of the impugned conveyance will be established under the proposed deeming provision by proving the "insolvency" of the debtor and the absence of fair and reasonable consideration (see *supra*, this ch., sec. 6(a)(iii)). Under these circumstances, the provision deeming prejudicial effect and the proposed saving clause are inextricably intertwined insofar as the factor of consideration is concerned. Since, under the deeming provision, prejudicial effect and, therefore, invalidity, would result where, *inter alia*, the consideration given for the property conveyed was not fair and reasonable relative to value of the property, the existence of such consideration would save the transaction. However, in certain circumstances, prejudicial effect may well be proven notwithstanding the existence of fair and reasonable consideration. In such a case, the conveyance would be voidable under what may be called the "basket" clause proposed *supra*, this ch., sec. 6(a)(iii), but not under the deeming provision; nevertheless, the proposed saving provision in respect of fair and reasonable consideration would operate independently to protect the conveyance.

(viii) Further Powers of the Court

Under the present provincial legislation, a court dealing with an impeached conveyance is restricted in its powers, in that it can either set aside the conveyance or affirm it. The absence of statutory jurisdiction to respond in a more flexible manner often hamstrings a court: it may have real doubts whether the debtor had a fraudulent intent, and must bear in mind that, by voiding the conveyance, the transferee may be left in the unfortunate financial position of having no automatic right to a return of the consideration. Under the proposed regime, where a conveyance may be set aside because of its prejudicial effect and where the transferee may have acted in good faith, the inequity may be seen to be even more pronounced.

The New Brunswick Report recommended that a transferee who gave "valuable" consideration and who "did not deliberately encourage or assist the debtor in furthering his intention to defeat creditors" should be entitled to a "return of any consideration he transferred to the debtor".[370] All other transferees would have their claims to a return of the consideration "postponed until all other creditors existing when the transaction is set aside are satisfied in full".[371] Section 9(2) of the Uniform Fraudulent Conveyance Act allows a purchaser who is without actual fraudulent intent and who has given less than a fair consideration to "retain the property or obligation as security for repayment". Under section 9(2), the transferee is accorded the right to refuse to give up the property until his claim to the consideration is satisfied, a right apparently not part of the New Brunswick proposals.

It is noteworthy that the drafters of Bill C-12 seem to have been prepared to go beyond a return of the consideration. In exercising its various powers under sections 169(4)(*c*), 169(5), and 175, the court is empowered to restore each party to the transfer in so far as possible to the state that he was in immediately prior to the transfer. It may be said that the power to restore the *status quo ante* "in so far as possible" gives the court a broad jurisdiction to do justice in individual cases.

The Commission is of the view that the general thrust of the existing or proposed legislation discussed above ought to form part of the panoply of powers to be accorded to a court. However, we do not believe that it is necessary to propose a statutory solution for each situation that may be envisaged. The circumstances will vary, in some cases quite dramatically, from case to case, so that detailed guidelines are not appropriate. Accordingly, it is recommended that the court should be empowered to make an order restoring each party to the conveyance, insofar as possible and equitable in the circumstances, to the position he was in immediately prior to the conveyance. For example, such restoration might be by way of retention of the property by the transferee as security for repayment, set off, or a first charge on the proceeds of a sale of the conveyed property.[372]

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[370] New Brunswick Report, *supra*, note 30, at 158-59.

[371] *Ibid.*, at 159.

[372] The Commission's recommendation respecting restoration of the *status quo ante* is

(ix) Recovery of the Property or the Proceeds

a. Recovery of the Property

Where an action to impeach a fraudulent conveyance is successful, the property conveyed is subject to the claims of creditors if still in the hands of the original transferee. However, the fact that a fraudulent conveyance is only voidable, and not void, means that the property cannot be recovered from a subsequent purchaser from the original transferee where that purchaser is a *bona fide* purchaser for value without notice of the original fraud.

With respect to a disposition of the property by the original transferee to a subsequent purchaser, the New Brunswick Report would "protect a subsequent *bona fide* purchaser for value without notice of the voidability of the transaction between the debtor and the other party".[373] Section 76 of the *Bankruptcy Act* permits recovery of the property from a subsequent purchaser, except where he has "given . . . in good faith adequate valuable consideration" for the property. Section 175(1)(*a*) of Bill C-12 permits recovery of the property from a subsequent purchaser, but section 175(2) provides that subsection (1) does not apply "where any person to whom property has been transferred paid or gave in good faith adequate valuable consideration for the property".

The Commission is of the view that existing provincial fraudulent conveyance legislation is inadequate because it does not deal expressly with the recovery of fraudulently conveyed property from persons who purchased the property subsequent to the original transfer. The Commission believes, and accordingly recommends, that, where a conveyance has been declared invalid – that is, where it has defeated, hindered, delayed, or defrauded creditors – creditors should be entitled to recover the property from a transferee subsequent to the original transferee except where the subsequent transferee acted in good faith and paid valuable consideration. The Commission further recommends that nothing in the new legislation should permit the recovery of the conveyed property from any transferee subsequent to a transferee who obtained the property from the debtor pursuant to a conveyance that would be protected under the proposed new legislation. In other words, where the original transferee is protected and obtains good title, we can see no reason why he should not be able to pass good title to anyone after him. Quite simply, further transfers should proceed as though the original conveyance had not been impugned at all.

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wider than the New Brunswick proposal dealing with "the return of any consideration . . . transferred to the debtor". If, prior to the voidable conveyance action, a creditor, for example, were to garnish money payable, but not yet paid, by the transferee to the debtor in respect of property conveyed to the transferee, the amount as garnished would not be "consideration . . . transferred to the debtor" that would be returnable under the above-noted New Brunswick proposal. A further New Brunswick proposal would protect the transferee in the above type of case, but only if the proceeds of the garnishment were not already distributed to the creditors. The Commission's restoration recommendation would, however, permit a court to restore the *status quo ante* in all situations, to the extent "possible and equitable in the circumstances".

[373] New Brunswick Report, *supra*, note 30, at 161.

b. Recovery of the Proceeds

Section 12 of the *Assignments and Preferences Act*, also applicable to proceedings under the *Fraudulent Conveyances Act*, permits the recovery from the original transferee of proceeds of the sale of property where the transferee "has sold or disposed of, realized or collected the property or any part thereof". Of course, the right to recover the proceeds of transferred property can be no greater than the right to recover the property itself. This principle is enshrined in section 12(1) with respect to the original transferee: in referring to a disposition of the property by him, it is provided that "the money or other proceeds may be seized or recovered in an action by a person who would be entitled to seize and recover the property if it had remained in the possession or control of the debtor or of the person to whom the gift, conveyance, transfer, delivery or payment was made".

The recovery of proceeds was also considered by the New Brunswick Report. As a matter of principle, the New Brunswick Report first reaffirmed the general thrust of the New Brunswick equivalent of section 12(1). However, its recommendations concerning the recovery from the original transferee of the "proceeds" of disposed property would apply only where the proceeds were still in the transferee's possession and where the transferee was not fraudulent.[374] The Report also recommended recovery of "the value of the property at the time it was transferred to" the transferee "in the case of a person who deliberately encouraged or assisted the debtor in furthering his intention to defeat creditors".[375] Presumably, the intent was to be more lenient with respect to the former type of transferee, although whether this intention would be realized depends on the nature of the property sold and whether it would appreciate in value very rapidly: in some cases, the "proceeds" of a subsequent disposition may far exceed the "value of the property" at the time of transfer; in other cases, the opposite would be the case.

The Commission has concluded that, as in the case of the recovery of the property itself, new legislation should provide expressly for the recovery of the proceeds of property transferred in fraud of creditors. The Commission, therefore, recommends that, where a conveyance has been declared invalid, the proceeds or the value of the proceeds received by the original transferee or any subsequent transferee of the property who has disposed of such property should be recoverable. However, the proceeds or the value of the proceeds should not be recoverable from any person who would have had a right to retain the property itself.

It bears emphasizing that the Commission's proposal, in referring to the value of the proceeds, would remove the limitation noted in the New Brunswick Report that, "[i]f the proceeds are mixed with other property in a way that they cannot be distinguished, they cannot be followed".[376] Our proposal would remove the limitation that "proceeds can only be followed as long as they remain 'in the possession or control' of the transferee",[377] a limitation preserved in the New Brunswick recommendation.[378]

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[374] *Ibid.*, at 160.

[375] *Ibid.*, at 161.

[376] *Ibid.*, at 136-37.

With respect to the term "proceeds", we recommend that it should be defined to include money or any other type of property received from any disposition of the property, as well as any insurance or similar moneys or proceeds received on account of the loss, destruction, or damage of or to the property. This proposal is consistent with previous Commission recommendations that would treat insurance and other similar proceeds in the same manner as the property itself.[379] However, we do recognize that, where insurance or other similar coverage has been effected in respect of the property in question, some premiums may already have been paid at the time when the insurance or other proceeds are sought to be recovered. Accordingly, to avoid unjust enrichment, we further recommend that, in these circumstances, premiums paid should be reimbursed in such manner as the court directs.

(b) RECOMMENDATIONS FOR REFORM: FRAUDULENT PREFERENCES

(i) The General Rule

While preferences – that is, conveyances by debtors to creditors to repay existing debts – form merely a species of a larger category consisting of conveyances by debtors generally, we believe that there are sound policy reasons why they should be treated separately from other types of conveyance. The distinguishing characteristic of preferences is the fact that they are conveyances to persons who, by definition, always provide consideration, that is, the antecedent debt. While dispositions of property for less than adequate consideration by insolvent debtors to third parties other than creditors quite rightly may be looked upon with considerable disfavour, payment of a pre-existing debt is obviously a normal and desirable activity. In fact, it is a common activity even for honest, but insolvent or financially embarrassed, debtors who seek to juggle their obligations and payments in order to keep their financial affairs afloat.

Theoretically, perhaps one might wish to invalidate all payments or transfers preferring a creditor by an insolvent debtor. Clearly, where the debtor does not have sufficient assets to pay all his creditors in full, the preference offends the basic principle of equality of treatment enshrined in both creditors' relief and bankruptcy legislation. However, it has been strongly urged that such a proposal would have profoundly adverse effects on normal and acceptable commercial activity.

At present, the *Assignments and Preferences Act* utilizes a pure "intent" test except within the special sixty day impeachment period under section 4(3), where a *prima facie* presumption of fraudulent intent arises if the effect of the transaction is to give a creditor a preference. In the Western provinces, the debtor's intent is not a material factor within the impeachment period; the only critical issue is the effect of the transaction.[380] This more radical approach, even if only in the context of the statutory impeachment period, tends to belie to some degree any dogmatic assertion that the business community could not live with a regime that was not premised on the debtor's fraudulent intent.

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[377] *Ibid.*, at 136.

[378] *Ibid.*, at 160.

[379] See Commission Report, *supra*, note 315, Part II, at 24-25, 88-89, and 184-87.

Section 73(1) of the *Bankruptcy Act* uses an "intent" test for preferences occurring within three months prior to bankruptcy. However, where the transaction is with "a person related to" the debtor, section 74 provides that the period specified in section 73(1) shall be twelve months. Section 73(2) provides for a *prima facie* presumption of fraudulent intent where the transaction has the effect of giving a creditor a preference. Sections 172 and 173 of Bill C-12 distinguish between arm's length and non-arm's length transactions. As a general proposition, the requirement to prove the debtor's insolvency and to prove his intent to give a preference is applicable to both types of transaction. However, where a transfer to a creditor is not at arm's length and where it occurs within the stipulated period of time prior to the filing of a petition, the transfer is deemed by section 173(2) and (3) to have been made with the intent to give a preference. An exception is made where, for example, the transaction occurred as part of "the normal course of affairs of the debtor in relation to the creditor". Where, however, this exception does not apply, and where the deeming provisions do apply, the debtor's intent is irrelevant, and a regime based fundamentally on the effect of the transaction is in place, since, in all cases, the insolvency of the debtor must be shown. If the debtor is insolvent, the effect of the preference must have been to prejudice the other creditors.

Bill C-12 concentrates on, and impliedly makes certain assumptions about, the nature of the relationship between the debtor and the preferred creditor, depending upon whether they deal with each other at arm's length. Presumably, underlying the distinction is the assumption that non-arm's length transactions generally are suspect or often smack of collusion or fraud, whereas arm's length transactions, almost by definition, are ordinarily in the normal course of business and presumptively fair and reasonable.

Having examined existing and proposed preference legislation in other jurisdictions, and having assessed the utility of the present Ontario *Assignments and Preferences Act*, the Commission has come to the conclusion that the existing regime does not satisfactorily promote the principle of equality, which, we believe, ought generally to govern the law respecting fraudulent preferences. Fraudulent preferences law should complement creditors' relief legislation, where, in the main, all unsecured creditors share *pro rata* in any distribution of the proceeds of enforcement. Like the present law relating to fraudulent conveyances, fraudulent preferences law is bedevilled by several presumptions and inferences of fraudulent intent. The statutory and judge-made rules are intertwined in what often appears to be a confusing pattern. Bearing in mind, then, the rights and protection of creditors and the normal and reasonable expectations of those engaged in commerce, we recommend that the existing legislation respecting fraudulent preferences should be repealed in favour of new legislation designed to further the general principle of equality among creditors.

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[380] See *supra*, this ch., sec. 4(a)(v).

Having proposed the repeal of the fraudulent preferences provisions in the *Assignments and Preferences Act*, it now remains for us to recommend a new course of development. In this connection, our previous discussion of, for example, the *Bankruptcy Act*, Bill C-12, and preference legislation in other Canadian jurisdictions offers several models for reform. In addition, one could envisage that fraudulent preference legislation should generally be uniform with the fraudulent conveyances legislation proposed earlier. This alternative would serve to invalidate any preference the effect of which was to defeat, hinder, delay, or defraud one or more of the debtor's creditors. Subject to any saving provisions that might be adopted, the intent of the debtor and of the preferred creditor would be irrelevant.

The Commission believes, however, that a regime based essentially on the effect of the preference in question, while promoting the principle of equality of treatment for creditors, would be unduly harsh and would severely disrupt reasonable commercial activity and expectations. Creditors cannot be expected to investigate and monitor a debtor's financial status each time they seek to collect their legitimate debts. The payment of an antecedent debt to a creditor therefore differs from the transfer of property to a person who is not a creditor. Consequently, any new preference legislation must effect some type of workable compromise between commercial practice and the laudable wish to do justice to all creditors where the debtor's financial position is precarious.

The Commission is of the opinion that such a compromise may be found in a preference regime akin to the one established under Bill C-12. We believe that a regime based on a distinction between arm's length and non-arm's length transactions between debtors and creditors would, more than other regimes, protect creditors, correspond with the realities and requirements of modern commercial activity, and conform to the reasonable expectations of both debtors and creditors. As we observed earlier, the distinction reflects the notion that certain kinds of relationship between debtors and creditors are inherently more suspect and, therefore, require more rigorous monitoring, while others bespeak a degree of independence that does not warrant so close a scrutiny. Finally, the distinction reflects, in one form or another, more or less well-known commercial and legal principles. Accordingly, the Commission recommends that new legislation respecting preferences should distinguish between arm's length preferences and non-arm's length preferences. More specifically, with respect to arm's length preferences, it is recommended that, subject to the provisions to be proposed below, a creditor should be entitled to have an arm's length preference set aside where (a) the debtor had the intent to give a preference, and (b) the preference had the effect of defeating, hindering, delaying, or defrauding one or more of the debtor's creditors.

In addition to the fact that the preceding recommendation concerning arm's length preferences effectively conforms to section 172 of Bill C-12 in its dual requirement of proving both fraudulent intent and prejudicial effect, the retention of the concept of fraudulent intent rests on what we believe to be sound philosophical and practical grounds. As we have stated, in the context of an arm's length repayment of a debt, the normal presumption is that the transaction is *bona fide* and reflects no more than normal and reasonable commercial practice. Caution must be exercised in seeking to strike down legitimate attempts to pay debts, even where, as a strict matter of causation alone, the payment amounts to a preference prejudicing other creditors. We say caution, however, not blindness. We, therefore, believe that a compromise is essential to balance the interests of both creditors and the commercial world. Whereas, in the context of fraudulent conveyances to persons other than creditors, we saw a need to be zealous in the protection of creditors, in the context of arm's length preferences we are of the view that policy and practicality necessitate the adoption of the dual intent and effect requirements proposed above.

With respect to a non-arm's length preference, section 173 of Bill C-12 requires, *inter alia*, proof of the debtor's insolvency and proof of his intent to give a preference. However, unlike the situation where an arm's length preference is given, section 173(2) and (3) deems certain preferences to have been made with the requisite intent if given within a stipulated period prior to the filing of a petition. Leaving aside exceptions to the deeming provisions, the impeaching creditor would have to prove insolvency alone under section 173(2) and (3). And, since a preference given by an insolvent debtor necessarily prejudices the remaining creditors, a regime premised essentially on the effect of the transaction has been established under section 173.

Having regard to the general principle of promoting equality among all creditors where the debtor cannot pay all of them in full, and having regard to the very nature of non-arm's length preferences, to which reference was made earlier, the Commission believes that new legislation should not impose a proof of intent requirement on an impeaching creditor in these circumstances. Rather, the focus should be exclusively on the effect of the preference. Accordingly, the Commission recommends that, subject to the provisions to be recommended below, a creditor should be entitled to have a non-arm's length preference set aside where the preference has had the effect of defeating, hindering, delaying, or defrauding one or more of the debtor's creditors.[381]

(ii) The Determination of the Effect of a Preference

For the reasons discussed in the context of fraudulent conveyance actions, we believe that the court should be provided with certain statutory guidance in respect of the determination of the prejudicial effect of a preference. This guidance should be consistent with that applicable to fraudulent conveyances, since both deal with analogous situations. Accordingly, the Commission recommends that legislation should provide that a preference has the effect of defeating, hindering, delaying, or defrauding creditors where the debtor was insolvent at the date of the preference.[382] As in the case of fraudulent conveyances, we do not wish to propose the adoption of rigid rules defining when a preference has a prejudicial effect. We, therefore, further recommend that legislation should make it clear that proof of insolvency should not be the only means of establishing that a preference had the effect described above.

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[381] Dissent by the Chairman, Dr. D. Mendes da Costa:

> In my view, the issue raised here is substantially similar to that already discussed in the context of fraudulent conveyances. For reasons noted in that context (see *supra*, note 353), I do not agree with the introduction of the "effect regime" proposed by my colleagues. I would support the type of regime described in my earlier dissent.

With respect to the definition of "insolvency", we recommend the enactment of the same type of legislation proposed for fraudulent conveyance actions. Accordingly, a person should be deemed to be insolvent where (a) he does not have sufficient property subject to enforcement measures to pay all his debts in full, if such property were sold at fair market value, rather than under legal process, or (b) he has ceased to pay his debts generally as they become due.

(iii) Statutory Presumptions

It will be recalled that, under certain circumstances, the *Bankruptcy Act*, Bill C-12, and the various provincial preference statutes employ presumptions and deeming provisions in respect of the debtor's intent. The Commission has already subscribed to the view that the law should be more cautious in striking down arm's length preferences than non-arm's length preferences. With respect to the former, section 172 of Bill C-12 requires proof of the debtor's insolvency and proof of his intent to give a preference, and there are no presumptions or deeming provisions. This position should be contrasted with the provisions in respect of non-arm's length preferences: section 173(2) and (3) deems certain transactions to have been made with the intent to give a preference, so that an impeaching creditor faces an easier task in seeking to set aside a non-arm's length preference.

The Commission has come to the conclusion that, on balance, the approach adopted in Bill C-12 is the correct one. That is to say, we believe, and accordingly recommend, that creditors seeking to set aside an arm's length preference ought not to be aided by any presumption or deeming provision with respect to the requirement to prove the debtor's fraudulent intent. Given the principle that such transactions ordinarily reflect reasonable commercial practice, and in order not to discourage the *bona fide* payment of just debts, we see no reason why an impeaching creditor should not have to prove fraudulent intent in the normal manner. Having regard to the nature of arm's length transactions, we are of the view that the requirement to prove such intent is simply too critical to warrant the introduction of a presumption or deeming provision.

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[382] Reference to inadequacy of consideration, which appears in the parallel fraudulent conveyances proposal, is not included: repayment of an antecedent debt always is adequate consideration, so that, if inadequacy were required to be proven, no preference would ever be invalidated.

However, the Commission is disposed to a somewhat different treatment regarding the requirement to prove the prejudicial effect of a preference, at least where the preference is not at arm's length. In this connection, it is recommended that, in any proceeding brought within six months of the date of a non-arm's length preference, there should be a *prima facie* presumption that the effect of the preference was to defeat, hinder, delay, or defraud one or more of the debtor's creditors. For the reasons canvassed earlier, however, no similar presumption ought to arise in respect of arm's length preferences. Again, the Commission has been mindful of the need to balance carefully the protection afforded to creditors and the legitimate interests of the business community.

(iv) The Determination of Arm's Length and Non-Arm's Length Preferences

We now turn to the means of distinguishing arm's length from non-arm's length transactions. The provisions in Bill C-12 relating to such transactions have been reproduced and discussed earlier.[383] We believe that the distinction occupies as central a place under our proposals as it does under Bill C-12 and, therefore, the legislation in Bill C-12 may be seen as a model for the provincial statute. Accordingly, we recommend that provisions similar to sections 7 and 8 of Bill C-12 should be enacted to define and delineate the nature and scope of arm's length and non-arm's length preferences under the proposed new legislation.

(v) Entitlement to Attack a Preference: The Definition of "Creditor"

The Commission now turns its attention to the definition of "creditor" for the purposes of the proposed preference legislation. In this connection, the Commission is of the view that the restrictive interpretation of the term "creditor" in the Ontario *Assignments and Preferences Act* – basically limiting its meaning to judgment creditors and, perhaps, non-judgment creditors with liquidated claims – ought to be overturned by express legislation. We are unable to endorse the traditional view that, almost by definition, a non-judgment creditor cannot be prejudiced by a preference given by an insolvent debtor. Indeed, the debtor may very well have intended to defeat that creditor. We believe that the issue concerning the effect of the transaction on a non-judgment creditor is best left to the courts. Accordingly, we recommend the enactment of legislation similar to that proposed in the fraudulent conveyance context. The term "creditor", insofar as it relates to the entitlement to impeach a preference, should be defined broadly to mean a person who, at the time of the preference, has a judgment or cause of action against the debtor, whether the claim in respect of the cause of action is liquidated or unliquidated, absolute or contingent, certain or disputed, or payable immediately or at a future time.

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[383] See ss. 7 and 8, reproduced *supra*, at 186-89.

With respect to creditors whose judgments or causes of action arose only subsequent to the preference in question, we believe that our recommendation should again be uniform with the recommendation made in the context of fraudulent conveyances. Accordingly, we recommend that, for the reasons advanced earlier, a subsequent creditor should not have a right to impeach a preference.

(vi) Protected Preferences

At present, section 5 of the *Assignments and Preferences Act* provides for various exceptions to the general rule in section 4(2) avoiding fraudulent preferences.[384] We now turn to consider each of these saving provisions.

The first such provision to which reference will be made is the exception for preferences made in the normal course of business of the debtor in relation to the preferred creditor. This type of exception is found in section 173(2) and (3) of Bill C-12 and in section 5(1) of the *Assignments and Preferences Act*.

The Commission believes that such a provision has an expressly commercial flavour to it and, therefore, ought to be preserved in an area of the law so vital to the business community. Accordingly, we recommend that a preference should be upheld and the preferred creditor protected in any case where it is shown that the transaction between the debtor and the preferred creditor occurred in the normal course of business or affairs of the debtor in relation to that creditor. In addition, to avoid rigidity in the application of our proposal, we recommend that this exception should not be restricted to cases in which the debtor and the preferred creditor have dealt with each other on a regular basis. Rather, the exception should be equally operative where the preference given by the debtor to the preferred creditor was the first occasion, after contracting the original debt, when the two parties dealt with each other. In the latter case, the court should have regard, for example, to the normal or commercially accepted conduct of parties in a position similar to that of the debtor and the preferred creditor.

In section 5 of the *Assignments and Preferences Act*, there are several provisions protecting transactions that involve the receipt of security by a creditor.[385] With respect to preferences coming within the purview of sections 5(4) and 5(5)(*b*), discussed together in an earlier part of this Report,[386] reference should be made to our recommendation, proposed below, dealing with the powers to be given to the court where a preference has been set aside.[387] This recommendation would permit the court to restore the *status quo ante* where, as is envisaged by sections 5(4) and 5(5)(*b*), the preferred creditor has given up his security in exchange for the impugned payment to him by the debtor. Accordingly, these two provisions would not be necessary in our proposed new legislation.

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[384] See *supra*, this ch., sec. 3(d)(iv).

[385] *Ibid.*, sec. 3(d)(iv)d.

[386] *Ibid.*, sec. 3(d)(iv)d.(1).

[387] See *infra*, this ch., sec. 6(b)(ix).

With respect to section 5(5)(*c*) of the *Assignments and Preferences Act*, which legitimizes a substitution "in good faith" of securities for the same debt "so far as the debtor's estate is not thereby lessened in value to the other creditors", the Commission is of the view that the provision reflects legitimate commercial practice. Accordingly, we recommend that the provision should be incorporated in the proposed new legislation.

There is one further specific exception to the general rule invalidating preferences, now appearing in section 5(5)(*d*) of the *Assignments and Preferences Act*, that the Commission believes ought to be retained – again, for reasons related to commercial expediency or necessity. We recommend, as did the New Brunswick Report,[388] that nothing in the new preference legislation should invalidate a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance in money is made to the debtor by the creditor in the *bona fide* belief that the advance will enable the debtor to continue his trade or business and to pay his debts in full and that the debtor will use the advance for these purposes.

Two matters arise in connection with the preceding recommendation. First, a small point concerning a slight change in language from present section 5(5)(*d*). Under our proposal, the creditor must honestly believe that his advance will not simply enable the debtor to rescue his business and pay his creditors, but that it will actually be used by the debtor to this end. Blind and reckless faith in an obviously fraudulent debtor will not suffice, however honestly the creditor is motivated. Secondly, we wish to note the retention of the requirement to prove the *bona fides* of the preferred creditor. Given the extraordinary nature of this exception to the general rule, and given the absence of any statutory limit placed on the extent of the security given up relative to the advance offered, we believe that the remaining creditors ought at least to be shown that the transaction was part of an honest, commercially reasonable, attempt to revivify the debtor's enterprise.

Another exception now included in section 5(1) of the *Assignments and Preferences Act* is "any payment of money to a creditor". As we have seen,[389] this exception is duplicative, at least in part, of another protective provision in section 5(1). In addition, if the "fair and reasonable" consideration proviso in section 5(1) does not modify the exception, it is both bizarre and far-reaching, since – assuming that "money" includes, for example, a cheque – most debts are paid in this manner. As a result, under the latter interpretation, if this exception were to be retained, the chances of successfully challenging a preference would be severely limited. If the section 5(1) proviso mentioned above is inapplicable, it is difficult to conceive of a compelling rationale for this exception in light of the purpose of fraudulent preference legislation. Accordingly, the Commission recommends that the exception for "any payment of money to a creditor" should not be included in the proposed preference legislation. Any payment of money to a creditor by a debtor should be treated in the same manner as any other method of satisfying an antecedent debt.

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[388] New Brunswick Report, *supra*, note 30, at 158.

[389] See *supra*, this ch., sec. 3(d)(iv)a.

A final protected transaction under the *Assignments and Preferences Act* to which reference will be made is the payment of wages by a debtor in accordance with the *Wages Act*.[390] In effect, section 5(5)(*a*) of the Act permits a debtor to pay his employees in priority to his other creditors, since the *Wages Act* gives such employees a priority in various circumstances, for example, in respect of the distribution of execution proceeds by a sheriff under the *Creditors' Relief Act*.[391]

Whatever may have been the state of the law respecting priorities at the time section 5(5)(*a*) was enacted, it cannot now be contended that only some, but not all, statutory priorities ought to be protected. A new provision should be adopted to permit such payments without fear of a subsequent fraudulent preference action. Accordingly, we recommend that nothing in the new preference legislation should invalidate or affect any payment or transfer of property to a creditor entitled by law to priority over other creditors, to the extent of the priority.

(vii) The Doctrine of Concurrent Intent

At present, in every fraudulent preference case, the plaintiff must prove that the preferred creditor had notice or knowledge of, or perhaps concurred in, the debtor's fraud. This doctrine operates independently of the exceptions in the statute. Clearly, in the context of non-arm's length preferences, where the debtor's fraudulent intent is irrelevant, it would be anomalous to retain the doctrine of concurrent intent. But, even in the context of arm's length preferences, where the debtor's intent is in issue, we believe that the doctrine would serve no useful purpose under the proposed legislation. The saving provisions that we have proposed provide, we believe, sufficient protection for the preferred creditor. If a creditor in receipt of an arm's length preference from a fraudulent and insolvent debtor cannot fit within these protective provisions, it is our view that his lack of notice or knowledge of, or complicity in, the debtor's fraud should not be sufficient to protect the transaction. Accordingly, we recommend that, subject to the recommendations protecting the *bona fide* substitution of one security for another security of equal value, and the granting of security for a pre-existing debt in exchange for an advance of money given in the *bona fide* belief that it will be used by the debtor to continue his trade or business and pay his creditors in full,[392] a preference should be voidable irrespective of the *bona fides*, intent, notice, or knowledge of the preferred creditor.

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[390] R.S.O. 1980, c. 526.

[391] R.S.O. 1980, c. 103. See *Wages Act, supra*, note 390, s. 3.

[392] See *supra*, this ch., sec. 6(b)(vi).

(viii) The Doctrine of Pressure

In a regime premised on the debtor's fraudulent intent, it is said that a debtor under pressure to pay a debt cannot, by definition, have such an intent if he succumbs to the pressure. Consequently, through harassment, for example, a preferred creditor may legitimize his preferred position over other creditors who have been willing to see the debtor through a difficult financial crisis. The *Bankruptcy Act* and legislation in virtually every Canadian province, including Ontario, have abolished the doctrine of pressure, at least within the special statutory presumption period. Prince Edward Island has gone even further: the doctrine of pressure has been abrogated generally for all preferences voidable under the *Frauds on Creditors Act*.[393]

As indicated in the context of fraudulent conveyances, the doctrine of pressure would have no relevance in a regime based on the effect of the transaction in question. As a result, under our proposals the doctrine would be inapplicable with respect to non-arm's length transactions. But the Commission rejects the doctrine generally, for reasons of policy, aside from the fact that its psychological underpinnings are somewhat contrived and suspect and that its very nature makes it difficult to employ in a particular case. Simply put, we believe that the doctrine may encourage harassment of debtors by over-zealous creditors to whom equality of treatment among creditors is of little or no importance. In this respect, the doctrine flies in the face of the basic thrust of preference legislation. Consequently, we recommend that a preference should be voidable whether the preference is given voluntarily or under pressure.

(ix) Further Powers of the Court

At present, the *Assignments and Preferences Act*, like the *Fraudulent Conveyances Act*, does not offer a court sufficient flexibility when setting aside a transaction. While there is less need for flexibility in the fraudulent preference context, since the preferred creditor's claim revives if the preference is set aside, we are of the view that new legislation should give to the court powers that are parallel to those given to the court in the fraudulent conveyance context.[394] Accordingly, it is recommended that, upon setting aside a preference, the court should be empowered to make an order restoring each party to the conveyance, insofar as possible and equitable in the circumstances, to the position he was in immediately prior to the date of the preference.

(x) Recovery of the Property or the Proceeds

The Commission is of the view that the rules respecting the recovery of property or proceeds in fraudulent preference actions should be uniform with the applicable rules proposed in the fraudulent conveyance context. Consequently, we recommend that, where a preference has been set aside, the property transferred should be recoverable from a transferee subsequent to the original transferee, except where the subsequent transferee acted in good faith and paid valuable consideration. We further recommend that nothing in the new legislation should permit the recovery of property from any transferee subsequent to a preferred creditor where the preferred creditor obtained the property pursuant to a preference that would be protected under the new legislation.

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[393] R.S.P.E.I. 1974, c. F-13, s. 2(1), (2), and (3).

[394] See *supra*, this ch., sec. 6(a)(viii).

With respect to the recovery of the proceeds, where a preference has been declared invalid, the proceeds or the value of the proceeds received by the preferred creditor or any subsequent transferee of the property who has disposed of such property should be recoverable. However, the proceeds or the value of the proceeds should not be recoverable from any person who would have had a right to retain the property itself. As in the case of fraudulent conveyances, "proceeds" should be defined to include money or any other type of property received from any disposition of the property as well as any insurance or similar money or proceeds received on account of the loss, destruction, or damage of or to the property. Where insurance or other similar coverage has been effected in respect of the property, and some premiums have been paid at the time when the insurance or other proceeds are sought to be recovered, the premiums paid should be reimbursed in such manner as the court directs.

(xi) Payment to a Guarantor, Surety, or Endorser of a Negotiable Instrument

Section 4(5) of the Ontario *Assignments and Preferences Act* provides as follows:

> 4.-(5) The word 'creditor' in the fifth line of subsection (2), in the second line of subsection (3), and in the second line of subsection (4), includes any surety and the endorser of any promissory note or bill of exchange who would upon payment by him of the debt, promissory note or bill of exchange, in respect of which such suretyship was entered into or such endorsement was given, become a creditor of the person giving the preference within the meaning of those subsections.

Section 73 of the *Bankruptcy Act*, which provides for the voiding of certain preferences to a creditor, provides that, "[f]or the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor".

It seems reasonable to reaffirm a provision like section 4(5). Accordingly, we recommend that the existing provision for treating payment to a surety or endorser of a promissory note or bill of exchange as the equivalent of payment to a creditor should be retained, but out of an abundance of caution it should be expanded to include payment to a guarantor, an endorser of any negotiable instrument, or any other person in a similar position in relation to the debtor.

(c) MISCELLANEOUS REFORMS

(i) Institution of an Action

In its *Report on Class Actions*, the Commission considered the manner in which a fraudulent conveyance or fraudulent preference action is instituted.[395] The present law was summarized briefly as follows:[396]

> At common law, if a creditor is not a judgment creditor and he wishes to impeach a transaction of his debtor as a fraudulent conveyance, the creditor must bring the action on behalf of himself and all other creditors of the debtor: see *Reese River Silver Mining Co. v. Attwell* (1869), L.R. 7 Eq. 347, 20 L.T. 163, and *Kroman's Electric v. Schultes*, [1970] 2 O.R. 548, at 553, 11 D.L.R. (3d) 425 (H.C.J.). If the creditor is a judgment creditor, it is not necessary, but is nonetheless permissible, that the action be commenced on behalf of all creditors: see *St. Gregor Mercantile Co. v. Halbach*, [1927] 1 D.L.R. 761, at 763-65, [1927] 1 W.W.R. 247 (Sask. K.B.). Moreover, in relation to the *Assignments and Preferences Act*, R.S.O. 1980, c. 32, and the *Bulk Sales Act*, R.S.O. 1980, c. 52, case law has stated that an action by a creditor to set aside a voidable transaction specified by those Acts should be brought on behalf of all creditors: see *Westinghouse Canada Limited v. Buchar* (1976), 9 O.R. (2d) 137, at 141-42, 59 D.L.R. (3d) 641 (C.A.), and *Interlake Tissue Mills Co. Ltd. v. George Everall Co. Limited* (1921), 50 O.L.R. 165, at 166-67, 64 D.L.R. 206 (H.C. Div.), respectively. Regarding creditors' actions under the *Fraudulent Conveyances Act*, R.S.O. 1980, c. 176, see *Prytula v. Prytula* (1980), 30 O.R. (2d) 324, 116 D.L.R. (3d) 474 (H.C.J.), and *Reicher v. Reicher* (1980), 20 R.F.L. (2d) 213 (Ont. Div. Ct.).

The reason certain types of creditors' actions must be commenced on behalf of the plaintiff and all other creditors, while others may be commenced in the name of the plaintiff alone, is rather complicated and unclear and, for our purposes, not essentially within the purview of this Report. Suffice it to note here the statement of Mackenzie J. in *St. Gregor Mercantile Co. v. Halbach*[397] that "[a]n investigation of the authorities would indicate that the above differences in procedure is [*sic*] historic and arises from the diversity of the legal sources from which simple contract creditors on the one hand and execution creditors on the other derive their respective rights to make such an attack". Unfortunately, the emphasis in the case law on the jurisdiction of the courts of equity, prior to the fusion of law and equity, to grant broad equitable relief in respect of fraudulent transactions in favour of judgment creditors only, and on the jurisdiction of the courts under 13 Eliz., c. 5, or its modern equivalent, gives very little, if any, indication as to precisely why the setting aside of a conveyance under the statute must necessarily involve an action on behalf of all creditors. Indeed, most of the cases simply refer to the "leading" case of *Reese River Silver Mining Co. v. Attwell*,[398] without more;[399] unfortunately, *Reese River* is a very brief, and rather cryptic, decision.

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[395] Ontario Law Reform Commission, *Report on Class Actions* (1982), at 846-47.

[396] *Ibid.*, at 846-47, *n.* 89.

[397] *St. Gregor Mercantile Co. v. Halbach*, [1927] 1 D.L.R. 761, at 763, [1927] 1 W.W.R. 247 (Sask. K.B.). See, generally, *ibid.*, at 763-65.

[398] (1869), L.R. 7 Eq. 347, 20 L.T. 163.

[399] The attempted explanation in *St. Gregor Mercantile Co. v. Halbach*, *supra*, note 397, is lengthy, but not substantially more illuminating.

Moreover, it is not entirely clear whether those voidable transactions suits that traditionally must be brought on behalf of all creditors are subject to the strictures of Rule 75 of the Supreme Court of Ontario Rules of Practice,[400] the governing class action provision in Ontario.

In practice, the failure to sue on behalf of all creditors is not an irreparable error on the part of an impeaching creditor. The courts have permitted plaintiffs to amend their documentation to include the necessary reference.[401]

In its *Report on Class Actions*, the Commission recommended that Rule 75 be repealed and that a new expanded class action procedure be implemented by statute. The proposed procedure would contain a number of prerequisites to judicial "certification" of the action as appropriate for class treatment.[402] These prerequisites would include, for example, a preliminary merits test and an adequacy of representation requirement.[403] In addition, the proposed procedure would contain provisions designed to safeguard the interests of absent class members, including a provision to the effect that a class action cannot be settled or discontinued or dismissed for want of prosecution without court approval.[404]

In its Report, the Commission questioned "whether some of the prerequisites of the proposed *Class Actions Act*[405] or, indeed, of Rule 75, should apply to creditors' actions".[406] The Commission deferred consideration of the question "whether and, if so, to what extent, [voidable transactions] suits should be subject to the proposed *Class Actions Act*", although it stated that, "[i]n the meantime, we are of the view that such actions should not be comprehended by the Act".[407]

The Commission has already noted that the existing law governing the institution of a voidable transaction suit in Ontario appears to be premised on jurisdictional matters formerly governing the courts in England that have nothing to do with the prevailing rules in Ontario. Moreover, as a matter of policy, we believe that it is anomalous for all *Assignments and Preferences Act* creditors to be required to bring their actions on behalf of all creditors, whereas *Fraudulent Conveyances Act* judgment creditors are given an option whether to do so or not. It is also anomalous, in our view, that, under the *Fraudulent Conveyances Act*, non-judgment creditors must sue on behalf of all creditors, whereas judgment creditors are not so required.

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[400] Supreme Court of Ontario Rules of Practice, R.R.O. 1980, Reg. 540 (hereinafter referred to as "Rules of Practice"). See *Report on Class Actions*, *supra*, note 395, at 847.

[401] See, for example, Rules of Practice, *supra*, note 400, rr. 132, 186, and 188.

[402] *Report on Class Actions*, *supra*, note 395, at 290-99.

[403] For a discussion of the proposed prerequisites to certification, see *ibid.*, chs. 7, 8, and 9.

[404] *Ibid.*, ch. 20.

[405] The Commission's Draft *Class Actions Act* appeared as Appendix 1 of its *Report on Class Actions*, *supra*, note 395.

[406] *Report on Class Actions*, *supra*, note 395, at 847.

[407] *Ibid.* See Draft *Class Actions Act*, *supra*, note 405, s. 56(*c*).

After careful consideration, the Commission has come to the conclusion, and accordingly recommends, that the present rules governing the institution of a fraudulent conveyance and fraudulent preference action should be abolished. Both judgment and non-judgment creditors should be entitled to commence an action to set aside a fraudulent conveyance or fraudulent preference either as individual plaintiffs or on behalf of all creditors. Where the action is commenced on behalf of all creditors, it should be required to be brought under the Commission's Draft *Class Actions Act* or, prior to the implementation of that Act, under Rule 75 of the Rules of Practice.

We see no reason why, unlike other potential plaintiffs, persons intending to impeach an allegedly fraudulent transaction, and who do not purport to act on behalf of others, ought to be forced to invoke the prevailing class action procedure. The result of their individual action will not bind other creditors. As our *Report on Class Actions* makes clear, there are both advantages and disadvantages to proceeding under the Draft *Class Actions Act*. For example, while the class representative would be able to take advantage of the court-supervised contingent fee rules,[408] he would also be required to establish the prerequisites to certification. The option to invoke the governing class action procedure or to proceed in an individual action should be left to the impeaching creditor.

(ii) Transfers of Exempt Property

In an earlier section, we noted that a fraudulent conveyance of exempt property cannot be impeached, since creditors could not have seized and sold the property in any event.[409] A similar rule applies with respect to exempt property conveyed to a creditor for a pre-existing debt. The Commission is of the view that the present law ought to be reaffirmed and, therefore, recommends that the proposed legislation concerning fraudulent conveyances and fraudulent preferences should not invalidate or affect any transaction involving property exempt from enforcement measures.

(iii) The Duty of the Sheriff with Respect to Fraudulent Transactions

There is some old authority for the general proposition that, "[i]f it be once established that the 13 Eliz. c. 5 is as available to the sheriff as to the execution creditor himself, it appears to follow that it is the sheriff's duty to discover a fraud committed under that Act, or be liable for the consequences of his not so doing".[410] Moreover, there was some suggestion that the sheriff would be under a duty to seize property that was the subject matter of an allegedly fraudulent transaction. The Commission believes that, while this issue is not of great significance in practice, any controversy ought to be put to rest.

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[408] *Report on Class Actions*, *supra*, note 395, ch. 17.

[409] See *supra*, this ch., sec. 2(b)(ii).

[410] Edwards, *The Law of Execution* (1888), at 148.

As indicated in Part I of this Report, at the present time the sheriff has no responsibility for the conduct of judgment debtor or third party examinations.[411] Creditors alone examine debtors and others and, by means of these examinations, attempt to obtain information concerning previous dispositions of property by their debtors, clearly with a view to possible voidable transactions suits. However, under the new regime proposed by the Commission, the sheriff, responsible for the operation of the new enforcement office in each county, would have responsibility for administering judgment debtor questionnaires and conducting judgment debtor and third party examinations.[412] Consequently, having regard to the usual questions asked of judgment debtors, the sheriff might well become aware of conveyances and preferences that might be impeachable.

The Commission is of the view that sheriffs ought not to be placed in a position of having to assess the legal validity of a disposition of property and then to act accordingly. We firmly believe that any action taken in respect of fraudulent conveyances or preferences should continue to be the exclusive province of creditors adversely affected by the debtor's activities. We, therefore, recommend that, subject to any questions concerning a disposition of property by the debtor asked by the sheriff at a judgment debtor or third party examination or included in a judgment debtor questionnaire, the sheriff should not be under any duty to discover or investigate the existence of an allegedly fraudulent conveyance or preference or to act upon his own view of the matter – for example, by seizing the transferred property prior to a setting aside of the transaction.

(iv) Limitation Period

At present, neither the *Fraudulent Conveyances Act* nor the *Assignments and Preferences Act* imposes a limitation period in respect of actions to set aside a fraudulent conveyance or fraudulent preference. Nor does the *Limitations Act*[413] fill the void. The New Brunswick Report recommended the adoption of a six year limitation period running from the date of the transaction.[414]

In its *Report on Limitation of Actions*,[415] the Commission proposed a general "catch-all" provision of six years for any action not specifically provided for in its proposed limitations statute or in any other statute[416] – a provision that would apply to an action to set aside a fraudulent transaction. Ordinarily, the limitation period would run from the moment the cause of action arose. However, the Commission also proposed an extension of time where an action is based on fraud; in such cases, time would not begin to run until the plaintiff has discovered the fraud or could have discovered it with reasonable diligence.[417]

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[411] Commission Report, *supra*, note 315, Part I, at 162.

[412] *Ibid.*, at 157-63.

[413] R.S.O. 1980, c. 240.

[414] See New Brunswick Report, *supra*, note 30, at 154.

[415] Ontario Law Reform Commission, *Report on Limitation of Actions* (1969).

[416] *Ibid.*, at 61-63.

[417] *Ibid.*, at 109-11. In the draft limitations legislation contained in the 1977 *Discussion*

Actions to set aside a conveyance or preference are actions based on fraud, and they would remain so even under the legislation proposed in this chapter. The fact that the cornerstone or critical jurisdictional factor of our proposed legislation is the effect of the transaction, rather than the intent of the debtor,[418] does not alter the essential character of the action, which is to set aside transactions in fraud of creditors.

Bearing this in mind, the Commission wishes to reaffirm the proposals it made in its *Report on Limitation of Actions*. We, therefore, recommend that the limitation period for fraudulent conveyance and fraudulent preference actions should be six years from the time the plaintiff discovered the fraud or could have discovered it with reasonable diligence.

(v) Binding the Crown

Throughout the Commission's Project on the Enforcement of Judgment Debts – and, indeed, in the past generally – the Commission has been of the opinion that legislation that governs private citizens should bind the Crown.[419] Indeed, the trend is discernibly away from according a special status to the Crown in this respect. In the context of fraudulent transactions, there would seem to be no reason why other creditors should suffer where a payment or conveyance to the Crown falls within the four corners of the proposed legislation. Accordingly, it is recommended that legislation implementing the foregoing recommendations in respect of fraudulent conveyances and fraudulent preferences should bind the provincial Crown. We further recommend that the Parliament of Canada should be requested to enact legislation to make the federal Crown subject to the proposed provincial legislation respecting fraudulent conveyances and fraudulent preferences.[420]

RECOMMENDATIONS

The Commission makes the following recommendations:

General

1. The provisions of the *Fraudulent Conveyances Act* dealing with conveyances in fraud of creditors and the provisions of the *Assignments*

Paper on Proposed Limitations Act, distributed for comment by the Ontario Ministry of the Attorney General, s. 6(3)(*d*) and (4) provided that, in an action "based on fraud or deceit", the normal limitation period "is postponed and does not commence to run against a plaintiff until he knows, or in all the circumstances of the case, he ought to know", (a) "the identity of the defendant" and (b) "the facts upon which his action is founded".

[418] Although intent remains relevant with respect to arm's length preferences.

[419] See, for example, Commission Report, *supra*, note 315, Part II, at 187, where the Commission recommended that the proposed exemptions from garnishment should bind the Crown. See, also, *Execution Act*, R.S.O. 1980, c. 146, s. 7(5), which provides that the exemptions from seizure under any writ bind the Crown.

[420] This proposal does not, of course, deal with the right of trustees in bankruptcy to utilize provincial voidable transactions legislation, a matter entirely separate from the one considered here. See Bill C-12, *supra*, note 8, s. 10(3).

and Preferences Act dealing with fraudulent conveyances and fraudulent preferences should be repealed, and a single new statute should be enacted in their place.

Fraudulent Conveyances

*2. As a general principle and subject to the provisions proposed below, a creditor should be entitled to have a conveyance by a debtor to a third party (not being a creditor) set aside where the effect of the conveyance was to defeat, hinder, delay, or defraud one or more of the debtor's creditors.

3. The term "conveyance" should be defined to include a gift, transfer, grant, assignment, alienation, bargain, delivery over, lease, charge, mortgage, encumbrance, payment, release, limitation of use or uses, and any other type of disposition of, in, to, or out of any right, title, or interest in real property or personal property of any kind, whether by writing or otherwise.

4. (1) Legislation should provide that a conveyance has the effect of defeating, hindering, delaying, or defrauding creditors where

(a) the debtor was insolvent at the date of the conveyance or rendered insolvent by the conveyance, and

(b) the consideration given for the property conveyed was not fair and reasonable relative to the value of such property.

(2) However, legislation should make it clear that proof of insolvency and lack of fair and reasonable consideration should not be the only means of establishing that a conveyance had the effect of defeating, hindering, delaying, or defrauding one or more of the debtor's creditors.

5. A person should be deemed to be insolvent where

(a) he does not have sufficient property subject to enforcement measures to pay all his debts in full, if such property were sold at fair market value, rather than under legal process, or

(b) he has ceased to pay his debts generally as they become due.

6. (1) The term "creditor", as it relates to the entitlement to impeach a conveyance, should be defined broadly to mean a person who, at the time of the conveyance, has a judgment or cause of action against the debtor, whether the claim in respect of the cause of action is liquidated or unliquidated, absolute or contingent, certain or disputed, or payable immediately or at a future time.

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* The Chairman, Dr. D. Mendes da Costa, dissents from this recommendation: see *supra*, this ch., note 353.

*(2) A creditor whose judgment or cause of action arose subsequent to a conveyance should not have a right to impeach that conveyance.

7. The proposed legislation should contain a protective provision to the effect that a conveyance by a debtor should not be set aside where the consideration given for the property conveyed was fair and reasonable relative to the value of the property.

8. A conveyance should be voidable irrespective of the intent of the transferee.

9. A conveyance should be voidable whether the conveyance is made voluntarily or under pressure.

10. Where a court sets aside a conveyance, it should be empowered to make an order restoring each party to the conveyance, insofar as possible and equitable in the circumstances, to the position he was in immediately prior to the conveyance.

11. (1) Where a conveyance has been declared invalid – that is, where it has defeated, hindered, delayed, or defrauded creditors – creditors should be entitled to recover the property from a transferee subsequent to the original transferee, except where the subsequent transferee acted in good faith and paid valuable consideration.

(2) Nothing in the new legislation should permit the recovery of conveyed property from any transferee subsequent to a transferee who obtained the property from the debtor pursuant to a conveyance that would be protected under the proposed new legislation.

12. (1) Where a conveyance has been declared invalid, the proceeds or the value of the proceeds received by the original transferee or any subsequent transferee of the property who has disposed of such property should be recoverable; however, the proceeds or the value of the proceeds should not be recoverable from any person who would have had a right to retain the property itself.

(2) The term "proceeds" should be defined to include money or any other type of property received from any disposition of the property in question, as well as any insurance or similar money or proceeds received on account of the loss, destruction, or damage of or to the property.

(3) Where insurance or other similar coverage has been effected in respect of the property, and some premiums have been paid at the

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* The Honourable Richard A. Bell dissents from this recommendation: see *supra*, this ch., note 368.

time when the insurance or other proceeds are sought to be recovered, the premiums paid should be reimbursed in such manner as the court directs.

Fraudulent Preferences

13. The provisions in the *Assignments and Preferences Act* dealing with fraudulent preferences should be repealed in favour of new legislation designed to further the general principle of equality among creditors.

14. New legislation respecting preferences should distinguish between arm's length preferences and non-arm's length preferences.

15. Subject to the provisions to be proposed below, a creditor should be entitled to have an arm's length preference set aside where

    (a) the debtor had the intent to give a preference, and

    (b) the preference had the effect of defeating, hindering, delaying, or defrauding one or more of the debtor's creditors.

*16. Subject to the provisions to be proposed below, a creditor should be entitled to have a non-arm's length preference set aside where the preference has had the effect of defeating, hindering, delaying, or defrauding one or more of the debtor's creditors.

17. (1) Legislation should provide that a preference has the effect of defeating, hindering, delaying, or defrauding creditors where the debtor was insolvent at the date of the preference; however, proof of insolvency should not be the only means of establishing that a preference had the effect described above.

    (2) A person should be deemed to be insolvent where

        (a) he does not have sufficient property subject to enforcement measures to pay all his debts in full, if such property were sold at fair market value, rather than under legal process, or

        (b) he has ceased to pay his debts generally as they become due.

18. (1) Creditors seeking to set aside an arm's length preference ought not to be aided by any presumption or deeming provision with respect to the requirement to prove the debtor's fraudulent intent.

    (2) In any proceeding brought within six months of the date of a non-

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* The Chairman, Dr. D. Mendes da Costa, dissents from this recommendation: see *supra*, this ch., note 381.

arm's length preference, there should be a *prima facie* presumption that the effect of the preference was to defeat, hinder, delay, or defraud one or more of the debtor's creditors; however, no similar presumption ought to arise in respect of arm's length preferences.

19. Provisions similar to sections 7 and 8 of the *Bankruptcy Act, 1980*, Bill C-12, 1980 (32d Parl. 1st Sess.), should be enacted to define and delineate the nature and scope of arm's length and non-arm's length preferences under the proposed new legislation.

20. (1) The term "creditor", insofar as it relates to the entitlement to impeach a preference, should be defined broadly to mean a person who, at the time of the preference, has a judgment or cause of action against the debtor, whether the claim in respect of the cause of action is liquidated or unliquidated, absolute or contingent, certain or disputed, or payable immediately or at a future time.

(2) A subsequent creditor should not have a right to impeach a preference.

21. (1) (a) A preference should be upheld and the preferred creditor protected in any case where it is shown that the transaction between the debtor and the preferred creditor occurred in the normal course of business or affairs of the debtor in relation to that creditor.

(b) The immediately preceding exception should not be restricted to cases in which the debtor and the preferred creditor have dealt with each other on a regular basis, but should be equally operative where the preference given by the debtor to the preferred creditor was the first occasion, after contracting the original debt, when the two parties dealt with each other. In the latter case, the court should have regard, for example, to the normal or commercially accepted conduct of parties in a position similar to that of the debtor and the preferred creditor.

(2) Nothing in the new preference legislation should invalidate a *bona fide* substitution of one security for another security for the same debt as long as the debtor's estate is not thereby lessened in value to the other creditors.

(3) Nothing in the new preference legislation should invalidate a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance in money is made to the debtor by the creditor in the *bona fide* belief that the advance will enable the debtor to continue his trade or business and to pay his debts in full and that the debtor will use the advance for these purposes.

(4) The exception for "any payment of money to a creditor", now in section 5(1) of the *Assignments and Preferences Act*, should not be included in the new preference legislation.

(5) Nothing in the new preference legislation should invalidate any payment or transfer of property to a creditor entitled by law to priority over other creditors, to the extent of the priority.

22. Subject to Recommendations 21(2) and (3), a preference should be voidable irrespective of the *bona fides*, intent, notice, or knowledge of the preferred creditor.

23. A preference should be voidable whether the preference is given voluntarily or under pressure.

24. Where a court sets aside a preference, it should be empowered to make an order restoring each party to the conveyance, insofar as possible and equitable in the circumstances, to the position he was in immediately prior to the date of the preference.

25. (1) Where a preference has been set aside, the property transferred should be recoverable from a transferee subsequent to the original transferee, except where the subsequent transferee acted in good faith and paid valuable consideration.

(2) Nothing in the new legislation should permit the recovery of property from any transferee subsequent to a preferred creditor, where the preferred creditor obtained the property pursuant to a preference that would be protected under the new legislation.

26. (1) Where a preference has been declared invalid, the proceeds or the value of the proceeds received by the preferred creditor or any subsequent transferee of the property who has disposed of such property should be recoverable; however, the proceeds or the value of the proceeds should not be recoverable from any person who would have had a right to retain the property itself.

(2) The term "proceeds" should be defined to include money or any other type of property received from any disposition of the property in question, as well as any insurance or similar money or proceeds received on account of the loss, destruction, or damage of or to the property.

(3) Where insurance or other similar coverage has been effected in respect of the property, and some premiums have been paid at the time when the insurance or other proceeds are sought to be recovered, the premiums paid should be reimbursed in such manner as the court directs.

27. The existing provision in section 4(5) of the *Assignments and Preferences Act* for treating payment to a surety or endorser of a promissory note or bill of exchange as the equivalent of payment to a creditor should be retained; however, out of an abundance of caution it should be expanded to include payment to a guarantor, an endorser of any

negotiable instrument, or any other person in a similar position in relation to the debtor.

Miscellaneous Reforms

28. (1) The present rules governing the institution of fraudulent conveyance and fraudulent preference actions should be abolished.

    (2) Both judgment and non-judgment creditors should be entitled to commence an action to set aside a fraudulent conveyance or fraudulent preference either as individual plaintiffs or on behalf of all creditors.

    (3) Where an action is commenced on behalf of all creditors, it should be required to be brought under the Commission's Draft *Class Actions Act* – proposed in its *Report on Class Actions* (1982) – or, prior to implementation of that Act, under Rule 75 of the Supreme Court of Ontario Rules of Practice, the present Rule governing class actions in Ontario.

29. New legislation concerning fraudulent conveyances and fraudulent preferences should not invalidate or affect any transaction involving property exempt from enforcement measures.

30. Subject to any questions concerning a disposition of property by the debtor asked by the sheriff at a judgment debtor or third party examination or included in a judgment debtor questionnaire, the sheriff should not be under any duty to discover or investigate the existence of an allegedly fraudulent conveyance or preference or to act upon his own view of the matter – for example, by seizing the transferred property prior to a setting aside of the transaction.

31. The limitation period for fraudulent conveyance and fraudulent preference actions should be six years from the time the plaintiff discovered the fraud or could have discovered it with reasonable diligence.

32. (1) Legislation implementing the foregoing recommendations in respect of fraudulent conveyances and fraudulent preferences should bind the provincial Crown.

    (2) The Parliament of Canada should be requested to enact legislation to make the federal Crown subject to the proposed provincial legislation respecting fraudulent conveyances and fraudulent preferences.

CONCLUSION

In the General Introduction to our *Report on the Enforcement of Judgment Debts and Related Matters*, appearing in Part I, the Commission stressed the need to establish a reorganized, comprehensive, and coordinated enforcement system. As an illustration of the deficiencies of the present regime, or regimes, we noted in Part II of our Report that existing enforcement remedies are not comprehensive in scope in that certain species of property remain immune from execution and garnishment. The Commission's objective was to rationalize the law relating to the enforcement of judgment debts – for example, by attempting to fill existing gaps in order to ensure that, except for certain exemptions, all assets in respect of which a debtor has some right, title, or interest are subject to enforcement.

The proposals made in this Part of our Report, dealing with prejudgment remedies and voidable transactions, are, in a sense, complementary to those made in Part II and described above: the recommendations in Part IV are designed to preserve for unsecured creditors property that might be or has been disposed of in order to defeat such creditors. A rationalized, comprehensive enforcement system would be cold comfort to creditors deprived of the fruits of their anticipated or actual judgments by the fraudulent disposition of non-exempt property by their debtors.

With respect to prejudgment remedies, the Commission has recommended the repeal, with one exception, of all existing provisional remedies and their replacement by a single new, more comprehensive, prejudgment remedy. In the same vein, the Commission has subjected the law respecting voidable transactions to a comprehensive and critical review, resulting in wideranging proposals for reform. In both cases, an attempt has been made to rationalize the law, bearing in mind the need to balance the interests of debtors, creditors, and other interested persons.

We wish to conclude Part IV by expressing once again our appreciation to Mr. Eric Gertner, Legal Research Officer, and Mr. M.A. Springman, Senior Legal Research Officer, as well as to Ms. M.P. Richardson, Counsel to the Commission, for their efforts in preparing this Part of our

Report. Finally, we wish to thank Mr. David E. Baird, Q.C., for his assistance during the Commission's deliberations relating to the issues considered in Part IV.

All of which is respectfully submitted.

Derek Mendes da Costa
Chairman

Allan Leal

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March 31, 1983

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